REPORT ON GERMAN CARTELS AND COMBINES 1946

VOLUME I

GERMAN ECONOMIC DECENTRALIZATION

An analysis of the
German Cartel and Combine Problem

DRAFT

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FOREWORD

The Decartelization Branch of the Office of Military Government for Germany (U.S.) was organized in December 1945 for the purpose of recommending and implementing policies, procedures and laws to advance the three basic objectives of decentralizing, deconcentrating, and decartelizing the German economy.

This report is based upon information gathered during the first year's activities of the Branch. It is submitted in draft form in the hope a fairly detailed discussion of the concentration and cartelization of German industry may be productive of comments and criticisms useful in shaping the future programs of the Branch. In the light of such criticisms as are received, this draft will be revised to present a brief yet comprehensive survey of the organization and operation of Germany's major combines, trusts and cartels.

Preparation of this draft has been under the editorial supervision of Charles C. Baldwin, Chief of the International Cartels Section, assisted by Henry M. Heymann and Blanche A. Robinson. The preliminary studies and comments on particular industries and combines were contributed by members of the respective industry sections, under the supervision of Francis W. Laurent, Assistant Chief of Branch for Deconcentration. Material on the enforcement program was assembled under the supervision of Johnston Avery, Assistant Chief of Branch for Trade Practices. The various references to I. G. Farbenindustrie are based upon material collected by the Control Office for I. G. Farbenindustrie under the supervision of Richardson Bronson, Deputy Control Officer and Assistant Chief of Branch for Field Control. The chapter on the German patent problem was prepared by Phillips Hawkins, Deputy Chief of Branch, and Otto Norton, Chief of the Patent Section, Control Office for I. G. Farbenindustrie. The summary of recommendations was prepared under the supervision of Creighton A. Coleman, Assistant Chief of Branch for Policy and Legislation.

Substantially every member of the staff has contributed to this report, many of them devoting their evenings and week-ends to its completion. In particular, mention should be made of the following staff members:

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N O T E

For a number of years the English-speaking peoples translated the German words Kartelle and Syndikate as "combinations", "trusts", "pools" or conspiracies in restraint of trade. As used in this report, Decartelization denotes a determined and organized effort to eliminate all Kartelle from the Germany economy, defining cartel as any business arrangement designed to limit, regulate or avoid competition. The term "arrangement" is used because it is broader than "agreement". Arrangements may be in the form of contracts, gentlemen's agreements, informal understandings, memberships in trade associations, control of co-operative or jointly-owned sales agencies designed to maximize the profits of the participants. In short, any formal or informal association of independent enterprises in the same or similar branches of industry, established with a view to securing a monopoly of the market is, by definition, a cartel.

For alternative definitions, see Appendix A of this volume.

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INTRODUCTION

Authorization

Determined to secure the future peace and well-being of mankind, the governments of the United States and Great Britain, acting through the President and the Prime Minister, (Atlantic Charter, Fourth and Fifth Principles) on 14 August 1941 agreed that:

> They will endeavor, with due respect for their existing obligations, to further the enjoyment by all states, great or small, victor or vanquished, of access, on equal terms, to the trade and to the raw materials of the world which are needed for their economic prosperity
>
> They desire to bring about the fullest collaboration between all nations in the economic field with the object of securing, for all, improved labor standards, economic adjustment and social security.

As a first step towards the implementation of these principles, Secretary of State Cordell Hull, on 20 April 1944, announced that an industry branch would be established in the Commodities Division of the Office of Economic Affairs of the State Department, in order that the responsibility for the Department's policy and acts on all matters relating to international industrial arrangements might be clearly fixed and properly coordinated. Five months later, in a letter addressed to President Roosevelt, Secretary Hull stated that the Department was preparing "definite policy proposals" for curbing international cartels; that in fact plans were under way for "discussions with other United Nations in respect to the whole subject of commercial policy." In his letter, Mr. Hull said further:

> The elimination of the restrictive practices of cartels is an objective that consistently follows from the liberal principles of international trade which this Government, under your direction, has consistently sought to implement through the trade agreement program and other aspects of commercial policy. It is also an objective which constantly follows from this country's traditional and long-standing program designed to protect the consumer against monopoly and to preserve individual enterprise on a freely competitive basis.

The program proposed by Mr. Hull had the full concurrence of President Roosevelt who, on 6 September

1944, directed the State Department to make certain that "defeat of the Nazi armies is followed by the eradication of these (cartel) weapons of economic warfare." The President's letter goes on to say that "cartel practices... will have to be curbed"; and it directs the State Department to continue its studies of cartels and cartel practices.

To give international sanction and authority to the decartelization of world trade as first proposed in the Atlantic Charter, the governments of the Soviet Union, Great Britain and the United States incorporated into the Potsdam Agreement (July 1945) as the basic law for Allied action in Germany the following two statements of policy:

> (A. 3. i) The purposes of the occupation of Germany by which the Control Council shall be guided are:
>
> The complete disarmament and demilitarization of Germany and the elimination or control of all German industry that could be used for military production.
>
> (B. 12) At the earliest practicable date, the German economy shall be decentralized for the purpose of eliminating the present excessive concentration of economic power as exemplified in particular by cartels, syndicates, trusts and other monopolistic arrangements.

Among the means specified for achieving this program, the Potsdam Agreement declared that Allied controls shall be imposed upon the German economy:

> To control German industry and all economic and financial international transactions, including exports and imports, with the aim of preventing Germany from developing a war potential and of achieving the other objectives named herein.
>
> To control all German public or private scientific bodies, research and experimental institutions, laboratories, et cetera, connected with economic activities.

Fifteen months later, determined to secure further support for the deconcentration and decartelization of German industry, the United States Government submitted to the United Nations in September 1946 a draft charter for an International Trade Organization, of which Chapter V read, in part, as follows:

Members agree to take appropriate individual and collective measures to prevent business practices among commercial enterprises which restrain competition, restrict access to markets or foster monopolistic control in international trade, and which thus have the effect of frustrating the purpose of the Organization to promote expansion of production and trade and the maintenance in all countries of high levels of real income.

Organization

To effectuate the purposes of the Potsdam Agreement with respect to the deconcentration and decartelization of the German industrial economy, the Office of Military Government, United States (OMGUS) on 15 December 1945 established a Decartelization Branch. The primary responsiblities of this Branch are (1) to disperse the ownership and control of those German industrial or business concerns which represent excessive concentrations of economic power, and to prevent their future reconsolidation; and (2) to eliminate German participation in cartels and prevent such participation in the future.

This program is, of course, a logical extension of the historic American policy in the field of industrial management. For over half a century, the Sherman Act has stood as a positive expression of the will of the American people to preserve freedom and equality of economic opportunity. In our experience only a democratically organized economy can provide the essentials for a full and good life. Totalitarian economies, organized from the top down, must resort to threats, bribes and subsidies to eke out a minimum standard of comfort for any save a privileged few; By preserving a free competitive market and a democratic system of industrial control, the United States has attained a high standard of living for management, labor and agriculture. But this standdard can be maintained only if government is alert to protest any infringement of the right to trade freely in world markets without let or hindrance from self-constituted groups seeking to control the production or distribution of essential commodities. For American industry is vitally dependent upon foreign supplies of various minerals and other strategic raw materials; and it is precisely these minerals and raw materials (tin, tungsten, nickel, chrome, mica, rubber, oil and high-grade iron ore) that are most subject to monopoly control.

Problem

That the heavy industrialists, perhaps more than any other group in Germany today, were hedging against military defeat is apparent from their actions. In 1944 meetings were held in Strasbourg

to lay post-war plans for a resumption of business as usual. These plans were referred to in a statement issued by the State Department in March 1945.

> The Department of State announced today that reliable information collected by Allied Governments clearly indicates that the Nazi regime in Germany has developed well arranged post-war plans for the perpetuation of Nazi doctrines and domination. Some of these plans have already been put into operation and others are ready to be launched on a widespread scale immediately upon termination of hostilities in Europe. Nazi Party members, German industrialists, and the German military, realizing that victory can no longer be attained, are now developing postwar commercial projects, are endeavoring to renew and cement friendships in foreign commercial circles and are planning for renewals of prewar cartel agreements. An appeal to the courts of various countries will be made early in the postwar period, through dummies, for "unlawful" seizure of industrial plants and other properties taken over by Allied Governments at the outbreak of war. In cases where this method fails German repurchase will be attempted through "cloaks" who meet the necessary citizenship requirements. The object in every instance will be to reestablish German control at the earliest possible date. German attempts to continue to share in the control and development of technological change in the immediate postwar period is reflected in the phenomenal increase in German patent registrations in foreign countries during the past 2 years. These registrations reached an all-time high in 1944.

It is of major importance to realize that this planning for an immediate postwar comeback was to be superimposed upon the economic penetration of neutral countries already far advanced before the surrender of May 1945. Operating chiefly through the international Swiss banks, Germany had disposed of more than ₤ 500 million of looted gold, using the proceeds to subsidize newspapers and carry on foreign propaganda, and to pay for war material. In addition, holding companies set up in neutral countries by Germany's major combines continued to operate throughout the war, while established subsidiary companies in neutral countries---particularly in South America--- were being expanded. The extent of these interests is presently unknown. However, the International Committee for the Study of European Questions estimated (January 1947) that in South America, Sweden and Switzerland alone, German citizens' personnal and corporate assets approximated ₤ 2 billion and that the bulk of this wealth remained in the possession of individuals and organizations retaining the nominal right to use it freely.

Let the Victor Beware

A dozen years after the termination of World War I the historians began piecing together the story of the attempts to disarm Germany under the terms of the Versailles Treaty. It was only then, from the vantage-point of 1930, on the eve of the Nazi seizure of power, that the magnitude of the failure became apparent. The historians of World War I and the architects of World War II synchronized their efforts with ironic perfection.

It is not enough to say that the attempt to disarm industrial Germany was a complete failure. Back of that failure lies the real story. The records of the period show that every device, every subterfuge, every instinct combined in the attitute of the German industrialists to prevent the accomplishment of the clear intention of the Allied statesmen. Germany emerged from the post-war period not the weakest but the strongest military power in all Europe, if not momentarily the strongest in the world. By her industrial power she once again within a generation was fully prepared to challenge the whole world, overrunning Western Europe and forcing war upon the United States. This apparent indestructibility of the German capacity for industrial war stands now against the background of history--very recent history. Twenty-seven years ago the statesmen of the victorious nations, recognizing the necessity for curbing the German will for power, laid down a policy of industrial control in their documents of peace. The failure then was not one of statesmenship but one of execution.

Now again the statesmen of the Allied nations have set down the policy of industrial disarmament in even stronger terms, and once again the burden shifts to those who must execute and implement the policies agreed upon. If to err is human the supposition must certainly be present that to make the same error twice is stupidity. To guard against that catastrophe there must be a full understanding of the previous mistakes.

The Failure of Versailles.

First, the Allied powers failed to appreciate the devious and ruthless character of German nationalism, rooted in history, stemming from the Hunnic invasions. After Napoleon's victory in 1808 Baron Stein summed up the German psychology to Frederick William III by counselling him that a treaty "binds the vanquished only within the limit where it cannot physically escape its effect." Again after 1920 it became all too obvious that the Germans felt bound by the Versailles Treaty only to the extent that their violations were detected and denounced.

Within a few years following World War I the Allied control over Germany's industrial potential grew weaker and weaker. The French General Nollet, Chief of the Allied Control Commission, testified that:

> The Government of the Reich tended... to weary the Allied Governments... to relax the vigilance of the Commission... to wear it out, and to lead it to desire its own departure. Under cover of this stubborn struggle, it (The German Government)... pursued the revival of its military power according to a previously determined plan....

Authority after authority has testified to the systematic plan of obstruction practiced by the Germans in their successful attempt to protect their industrial war potential against foreign supervision or control. There were studied programs of dilatory preliminaries, documents and records were "lost," Allies were "played off against each other" on questions of control; there were countless instances of duplicity deceit, guile, misrepresentation and, in many well documented instances, outright falsification.

The Germans, understandably enough, are dedicated to the proposition that the preservation of their industrial power is a sacred trust, that all attempts to curb that power must be opposed, and that any means are fair which aid in reestablishing them in a position to defy outside interference in their affairs. Allied officials, while rejecting such claims in principle, gravitate to the doctrine that it is more important to restore German industry than to direct every effort toward the protection of the next generation from a third world war. This clash of interests is in itself tragic, confusing the issue, since guarantees of peace do not preclude the creation of a healthy and prospering German economy. In the midst of a devastated country the threat of aggressive war may appear remote, whereas the problems of an impoverished people are ever present. This, plus the inescapable "business as usual" philosophy, stimulates the desire to revive German business now and postpone until later all safeguards against some future war.

Every organ of German expression is encouraging such a program. It is being said now, as it was said in the early 1920s, that Germany is a vital cog in the wheel of world prosperity, that Germany is a necessary customer, that an industrial Germany is needed to balance the conflicting interests of geographic ideologies, that the United States must assist in German recovery to relieve the tax burden at home. It is neither pertinent nor necessary to argue with these theories. It is sufficient merely to recognize the clear objectives of the mission, which state in unequivocal terms that the primary purpose is to render Germany incapable of another aggressive war and that recovery must proceed along lines consistent with this overriding objective. No contemporary cost can be mentioned in the same breath with the immeasurable cost of another world war. To argue that the taxpayers of the United States object to any price short of the total disarmament and deindustrialization of the German economy is to miss or to misrepresent the temper of the American people.

Decartelization and U.S. Trade Policy

The policies of Military Government calling for elimination of cartels are sometimes questioned as to their possible effects upon the efficiency of the German economy. These questions call for a restatement of U.S. policy against a background of the long-range objectives which the deconcentration and decartelization policy in Germany was designed to serve.

Certain fundamental issues are becoming clear. Mr. Bevin, in his speech of 22 October 1946, proposed a political pattern for Germany which closely resembles the federal union of the United States and made firm remarks about the need for eliminating trusts and monopolistic practices in Germany. Nevertheless, in becoming specific, he presented a complex proposal for the centralization and socialization of the German economy. This came at a time when the United States and British were discussing separately two important subjects: (1) Economic unification of zones in Germany, and (2) Proposals for revival of multilateral world trade through the I.T.O. Comparing our respective positions, it would appear that the British are trying in Germany to steer a hazardous course between nationalization and socialization, while the United States is working in the field of international trade to institute measures which will relax artificial controls and free these channels from the restraints of tariffs, cartels and other restrictive fiscal and trade policies.

However, it must be clear that United States policy is not simply a negative one. True, the Potsdam Agreement and JCS 1067, being concerned immediately with the control of Germany and the prevention of future aggression, did place emphasis upon demilitarization, denazification, decentralization, decartelization and other surgery to eliminate conditions resulting from the war and from the deeply entrenched alliance of many years' standing of German warmongers, Junkers, financiers and industrialists. A desirable restatement of policy would place these negative aspects against a background of the constructive policies under the influence of which these particular remedial provisions were instituted. A start in this direction may be made by reference back to President Roosevelt's letter to Secretary Hull of 6 September 1944 which points out the contrast between the long standing U.S. economic policy, in harmony with democratic political institutions, and the regimented cartels system of Germany.

Before the end of hostilities it was clear that if world peace was to be lasting, positive measures promoting multilateral world trade would have to be paralleled by common action to eliminate trade barriers, cartel practices, establish exchangable monies etc. which would have to be accompanied by full employment and full production in all countries of the special products which each is peculiarly able to produce most economically. Accordingly, the recently announced U.S. proposals for a World Trade Charter approved by 17 other United Nations at the London Conference in November 1946, contain the highly important provisions for the

elimination of restrictive practices in international trade for the purpose of promoting a greater degree of wholesome competition and a greater volume in international exchange of goods by insisting on fair play in international trade.

It will be important to prevent the injection, into this program, of proposals for international cooperation among private groups on terms which would empower them to make international economic agreements which would, in fact, carry out a contrary policy. The anti-trust laws do tend to keep American companies free of restrictions on production and trade. Before the war, however, in spite of legal handicaps, U.S. business moved toward protected domestic markets, high profits, and low turnover. It is not necessary to refer to the volumes of evidence gathered during and after the war, showing the results of this drift away from the long term democratic policy of the U.S. and toward the cartel patterns which some business men found attractive. At the same time, the U.S. economy as a whole proved, during the war, that technology in production could be developed independently in the United States under proper incentives, and that dependency on the technology of a cartel system was far from inevitable.

European developments before the war heightened the contrast of policies. Cartels, commercial treaties between private governments, were only a prelude. The industrial system of Europe tightened its internal structure. It regimented everything it touched. It showed the cartel world as a closed world in which the individual disappears; a hierarchical world of power politics in which giant concerns, acting for their subordinate firms, friendly and buffer states, trade and maneuver.

Whether this makes for efficiency is doubted. Neither private groups nor government regulatory bodies, (such, for example, as public utilities commissions), are known in general to fix low prices or high quality. Yet the efficiency of the economic system must be measured in terms of the ultimate consumer, not of the producer or middleman as such. If the profits of supposedly efficient operation are not passed on to those who deal with the efficient concerns, there is no substantial public advantage in greater efficiency; and the apparent economies are in many cases more than offset by the bureaucratic demands of a complex organism.

All this appears to demand a clear restatement of the principle that democracy cannot long survive the disappearance of economic democracy; and that the ability of individuals and moderate-sized groups to exchange goods in competitive markets is perhaps the least easily perverted mechanism for the correlation of productive effort with the needs of the people. To retain the clarity of the issues now being faced, it will be necessary to make clear the U.S. position that national and international restrictive arrangements are intimately

related. Unless there is an international cartel, the power of a group in a given country is limited by foreign competition, subject, of course, to whatever protection tariff policies and transport cost may provide. Conversely, unless there is a domestic cartel, in each of the producing countries represented in the international cartel, the international group will be weakened to the extent that independents compete in the cartel dominated markets.

With respect to Germany, it is clear that the manner in which the totalitarian character of the economy is liquidated and an alternative to totalitarianism is established must be consistent with the democratic objectives of encouraging freer trade among nations. Germans have long emphasized the need for equal access to the world's raw materials but in the past have denied their European neighbors equal access to raw materials in Germany, especially coal. The German problem, therefore, is not merely to revive German industry so as to reduce the burden on the U.S. taxpayer, but to re-establish the European economy in such a way that Europe as a whole can take its place in world trade. It is therefore important, for example, in making new arrangements for export of German products, that Military Government make sure that pre-war relationships between German firms and their previous foreign customers are not simply re-established along the same lines. Likewise, within Germany, the means taken to revive German production must not again centralize and weld together the German economy into a single instrument presenting a solid front of controlled economy against those nations which might otherwise be willing to relax trade restrictions along the lines suggested in the proposed World Trade Charter.

Program.

It is one thing to outlaw the German cartels and break up the combines now in control. It is another thing to prevent their return to power. Unless adequate measures are taken to preserve a competitive economy in Germany by vigorous enforcement of the Decartelization Law, the complexes will reassert their authority. For it is in the nature of the German industrial system to drift toward bigness and centralization.

The success of decartelization will be measured in direct proportion to the vigor of its enforcement. It is neither self-enforcing nor can its enforcement, in the initial stage at least, be left to the Germans. The procedure necessary for the detection of violations is a new function and, therefore, must be precedent-building rather than precedent-following. First the concentration of economic power must be dissolved and secondly it must be prevented from reassembling. The proposals for meeting the second objective are the immediate concern of the Enforcement Program.

Unlike the situation found in countries, accustomed to doing business under the free compe-

titive system, it is not likely that many voluntary complaints will be made in Germany. It is more likely that those subsidiaries which are broken off from parent companies will have a greater tendency to get back into accustomed associations than to resist, and consequently to complain against the efforts of the monopolistic companies to take them back. It will probably develop, therefore, that the independent concerns which the laws seek to protect, will resist the protection to a greater extent than they will resist the injury.

Therefore vigorous action must be taken to convince the German people that democracy, particularly economic democracy, is the most favorable medium for the full and complete development of an individual. Totalitarian tyrannies having failed to create and maintain a stable peaceful economy, the Germans must concede that the best possible economic system is one in which the material success of the individual depends primarily on his ability to contribute to the economic satisfaction of others; that the resulting philosophy of the individual is one of self-reliance, self-confidence, modified by the necessity to adjust and contribute to the needs of the community. It is assumed that such an individual will exercise an alert and effective control over his government and will compel that government and its officials to act for the general welfare (Volksgemeinschaft) rather than in the selfish interests of some special class. Just as the Germans must be convinced of the unsoundness of making irrevocable grant of political power to a dictator, so the German people must be convinced of the unsoundness of making an irrevocable grant of economic power to private persons, agencies or trusts.

Apart from an educational program there is being established a technical enforcement procedure. The task of maintaining an adequate surveillance, as distinguished from over-all enforcement over the whole body of German industry, is the primary goal. Enforcement, therefore, must be a process of sampling rather than a frontal attack. To accept any other premise would be a departure from reality. Decartelization is not punitive, nor is the enforcement of the decartelization program to be carried out in a punitive manner. The sanctions, however, are punitive. They provide for fines and imprisonment, and they must be so applied as to:

1. Show that decartelization is more than a gesture,
2. That it will be enforced no matter in what industry, or against whom and
3. That fines will be sought for minor violations, and imprisonment urged if it is deemed necessary to remove the violator from economic life.

Enforcement can be successful only if it is correlated and geared to the actual conditions as now existing in Germany. For that reason it is necessary to evaluate the trends of the immediate and more remote future. Among the conditions which must be considered are the economic, political

and social situations. Out of those considerations can come the evaluation of the temper of the people, their institutions, and their reaction to enforcement. Unless the German people ultimately accept this new economic concept of industrial as well as political democracy the victory will never be completely won.

The Germans, of course, are counting on the fact that the recovery of Germany (which they insist upon interpreting as a return to the status quo ante bellum) is a prerequisite for the recovery of Europe and the maintenance of a healthy world economy. They dismiss as of no relevance the fact that German industry and German manpower are a war potential of immediate concern to all of us so long as the German economy can be regimented or administered as a unit, either by private owners or by a central government. This war potential can only be reduced or controlled: (1) if the German government, whether imperial, republican, or socialist, cannot exercise undisputed tactical and operational control over the whole economy; (2) if common action, whether economic or political, depends upon obtaining the consent of thousands of people and independent enterprises. In other words, a peacefully expanding world trade is dependent upon the decentralization of German industry, the outlawing of all cartel and combine agreements, and the fixing of responsibility upon producing units locally owned and managed. This decentralization program must take place before any final central government can be organized on a federal basis.

It must be remembered that after the military collapse of the Kaiser and Reich in 1918, the United States Alien Property Custodian declared:

> Industrial Germany was in control of Imperial Germany. Industrial Germany sympathized and participated in the preparation for this war. Industrial Germany waged this war. Industrial Germany was the first to see defeat and force the military peace, in order that, with her industrial equipment intact, she might continue that same war by intensified and concentrated economic measures. Her ambitions are the same in peace and in war. Her methods are the same in peace and in war. Destroy your business competition by state aid, cartel combinations, dumping, full-line forcing, bribery, theft of patents or inventions, espionage, and propaganda.

With minor changes, these same words might be used to define the aims and aspirations of industrial Germany, 1933-1946 under National Socialism.

THE GERMAN PATENT PROBLEM

Patents, not Nazi agents, were Germany's real "fifth column," operating in advance of Hitler's armies to curb the war potential of all who might oppose the Reich's demands for lebensraum. Patents are legal monopolies granted for a limited time, intended as a stimulant for inventors and as a reward for disclosing inventions which might otherwise remain secret. Practically during the past quarter century, Germany has developed an entirely new patent technique, an entirely new use for patents and inventions, and has applied this new technique to implement her bid for world power. The idea was to make Germany a collecting-point for technical information gathered from the four quarters of the globe; to secure a "corner" on new industrial developments and thereby force the rest of the world to depend upon German inventions and technical "know-how"; and finally to maneuver foreign industry into serving the will of Germany's political and industrial leaders.

Patents and patent applications were the primary form in which German technology was packaged for export. A second method provided for exchange of "know-how," often based (viz.: dynamite, analine dyes, celluloid, bakelite, vitamins, etc.) upon foreign inventions. This much accomplished, cartel agreements were negotiated with a view to allocating world markets, fixing prices and setting restrictive sales and production quotas. Within a very few years Germany came to control the flow of technological information in many fields outside Germany. Owing to her capacity for and interest in research, Germany soon showed a favorable "trade balance" in this new export commodity: technology. In other words, Germany balanced the imports of technological data with but a fraction of her own technology, using the remaining surplus of exportable technology to bargain for special privileges abroad. In addition to money credits, these privileges included: access to information on war materials and equipment; production restriction of foreign industry, particularly war essential industry; fixing of exorbitant prices for certain equipment essential for war production, such as machine tools, in order to retard foreign industrial development and achieve a corresponding reduction of war potential; territorial restrictions, to name only a few. In this way, German industrialists subjugated foreign countries in technological fields without the use of arms; without financial power, which was lacking in Germany, and without control of important sources of raw materials which Germany likewise lacked.

Put another way: where once economic power was based on wealth in raw materials, fertile acreage, well-developed transportation facilities or financial predominance (all fields in which Germany was relatively poor), German industry shrewdly and purposefully set out to monopolize the flow of technological information and thus achieve international power. This strategy was based on the valid recognition of an essential

factor of this technological age, namely, the need for a continuing flow of new inventions, improved processes and technological "know-how." Thus, while realistically evaluating her own limitations (relative poverty in natural resources, gold and foreign exchange), Germany overcame this defect by concentrating on a strategy of obtaining domination and control over the methods and means of converting other people's natural resources and money into the machines and goods in greatest demand whether they be high-speed steels, pharmaceuticals, dyestuffs, cameras, synthetic fibers or weapons of war.

At the beginning of World War II, Germany was well on the way to becoming the repository of chemical, electrical and other technical information for manufacturers all over the world. This process was greatly facilitated by the fact that manufacturers outside Germany were all too often ready to cooperate, preferring to share in the financial benefits promised under German patent cartels rather than risk investment in perhaps unprofitable research work or enter into litigation to dispute Germany's right to control.

Now, at the end of World War II, we find unchanged the situation which allowed Germany to use control over the international flow of technical information for her own purposes. We have destroyed Germany's war machine and reduced a goodly portion of Germany to rubble; but unless methods and means are devised to prevent Germany from regaining control over the exchange of technological information, we must prepare for a revival of the old abuses, ending perhaps in another war.

There can be, of course, no thought of restricting the export of German technical knowledge. On the contrary, Germany must be compelled to disclose all her industrial and trade secrets to the rest of the world. What has to be controlled is the medium of exchange which Germany shall receive in compensation. Clearly, payment must not be in the form of control, whether formal or tacit, of which the three main contributing factors were:

(1) Patent Agreements
(2) "Know-how" Agreements
(3) Cartels

Patents were the backbone, the trunk of the widespreading tree, from which the "know-how" depended and upon which the exchange of technological information was based. "Know-how" (which is more intimate information than patent data and hence less susceptible of communication than the latter) was usually made a special part of cartel arrangements. The technique of controlling the flow of technology was not applied in solitary and rare instances, but was carried out by German Big Business, with the aid of the German Government, all along the line. Small wonder that Germany, in her bid for power, has favored cartelization of her industries for decades. Less wonder yet that an evil regime like that of the Nazis used the international power created by these cartels for its own sinister ends. In broad outline, this novel technique of exporting and dealing in technical information and patent rights operates as

follows:

An industrial field at home is cornered by means of patents, patent pools, cartel agreements, "Interessen Gemeinschaften" (communities of interests) and other trade restraining arrangements. Foreign patents are obtained and international cartel arrangements made to complement the domestic picture. A large amount of technical information--patented as well as unpatented--is the stock-in-trade. Patents can be licensed to firms which cooperate and used as a club over recalcitrant independents, while unpatented information can be traded away as "know-how" as soon as cartel relations become more intimate.

Case Histories

I.G. Farbenindustrie A.G. of Frankfurt M., Germany

During World War I, "Badische-Anilin & Sodafabrik," "Bayer," "Agfa," "Meister, Lucius & Bruening" (Hoechst), "Griesheim Elektron," and "Chemische Fabriken vorm. Weiler - ter Meer" formed an "Interessen Gemeinschaft" (community of interests) without relinquishing their formal independence. In 1925, a complete merger occurred and this loosely knit confederation was replaced by a single corporation named "I.G. Farbenindustrie A.G." The patent rights of each component organization were transferred to the new corporation, which embarked upon an extensive research and development program. Seven Patent Departments were set up to handle the patent work for the combine. The patent personnel alone consisted of more than 250 employees, while the average annual patent budget amounted to approximately RM 6 million. The following table shows the number of I.G. Farben patents in force, in Germany and abroad, in the years from 1932 through 1941:

	Patents	
Year	Germany	Other Countries
1932	5059	20,902
1933	5176	21,676
1934	5340	22,512
1935	5322	23,973
1936	5579	25,766
1937	5774	28,117
1938	5790	30,772
1939	5817	32,794
1940	5964	31,988
1941	6126	32,891

This list does not include pending patent applications which annually numbered many thousands. Patent applications filed by I.G. Farben from 1932 to 1943 were as follows:

	Patent Applications	
Year	Germany	Other Countries
1932	1383	3285

(cont'd)

Year	Germany	Other Countries
1933	1234	3696
1934	1394	4114
1935	1386	4538
1936	1546	6128
1937	1895	6040
1938	2174	5501
1939	1771	4285
1940	1498	1792
1941	1750	2549
1942	1844	Not Available
1943	1574	4506

A further breakdown of these figures would show that I.G. Farben divided its technology and production into three main groups ("Hauptsparten"): Group I covered nitrogen and hydrogenation; Group II covered the general chemical field, including inorganics, intermediates, plastics, buna, solvents, dyestuffs, auxiliaries, pharmaceuticals, insecticides and perfumes; Group III covered photographica and artificial fibers.

The following table gives a breakdown according to technological fields, and indicates the patent coverage enjoyed by I.G. Farben in the years 1932 and 1941:

Year		Patents Germany	Patents Other Countries
1932	Group I	565	3,254
	Group II	3,635	16,275
	Group III	859	1,373
1941	Group I	871	2,966
	Group II	4,182	25,459
	Group III	1,073	4,466

The total number of German patent rights, which were formerly owned by I.G. Farben and are still in force now, is estimated at approximately 18,000. A breakdown of this figure is as follows:

In 1942, when the expiration of patents was suspended, there were about--

6,100 patents in force
7,400 applications pending

Since that time, filed and now pending, about- 4,000 applications pending
Total (Approximate) 17,500 Patent rights in Germany

This patent empire was further increased by tens of thousands of foreign patents and patent applications and many thousands of patent licenses. In addition, there exist in excess of 30,000 I.G. Farben trade-mark registrations and applications for registration, as well as miscellaneous other industrial property rights, such as "Gebrsuchsmuster" (petty patents).

This enormous number of patents, patent applications and other industrial property rights, bolstered by an

almost infinite number of "know-how" exchange agreements, gave to I.G. Farben a controlling voice in the management of whole industries at home and abroad. For example, I.G. Farben exercised 100 per cent control over the domestic production of synthetic gas and oils, dyestuffs, explosives, synthetic rubber ("Buna"), methanol, cellophane and others, and a major voice in their world-wide distribution and sales. Indeed, its technological empire was so vast that like an absolute ruler it could grant or withhold from others, in Germany and in other countries, the permission to enter any of its protected fields. The case of acetic acid is typical:

Acetic acid is one of the more important heavy chemicals used by industry. The United States consumes 335,000,000 pounds of it in a single year. The largest single outlet is in the manufacture of cellulose acetate which required 140,000,000 pounds of acid in 1941. Cellulose acetate is the raw material used in manufacturing rayon, safety photographic film, synthetic fibers and plastics. The second largest field of consumption is solvents, which are used in making paints, lacquers, and varnishes. These two broad categories account for over three-fourths of American consumption of acetic acid. Other important uses of this chemical are in the manufacture of pharmaceuticals, particularly salicylic acid, which is aspirin, and salvarsan. It is also used in the manufacture of dyestuffs, such as indigo, in the printing and dyeing of textiles, and in the tanning of leather.

Patents were instrumental not only in delaying the establishment of the synthetic acid industry but also in hampering the subsequent development. During the early 1930's, I.G. Farben held the United States patents on a new and promising process for making acetylene the principal material used in the manufacture of synthetic acetic acid. By an adroit manipulation of these patents and by a clever use of its partnership with Standard Oil of New Jersey, I.G. Farben succeeded in preventing the full development and utilization of that process. How I.G. Farben kept this process on the shelf while the demand for acetic acid was rapidly expanding is a complex but revealing story. It shows how United States patents in the hands of a foreign interest, such as I.G. Farben, became a menace rather than a boon to the chemical progress of the country. It further illustrates the harmfulness of such international partnerships as the chemical patent pool between I.G. Farben and Standard Oil of New Jersey.

At Baton Rouge, research was conducted by a Jasco staff which was composed of both Standard Oil and I.G. Farben people. But in Germany, I.G. Farben conducted its research without the direct participation of Standard Oil technicians. The results of such research were available to Standard Oil only insofar as I.G. Farben saw fit to report them. In that connection, it is significant that Standard Oil cautiously qualified its reference to the progress being made in Germany with the phrase, "so far as we know."

I.G. Farben apparently made no pretense of keeping Standard Oil, or even Jasco, up to date on the German

research being done on the acetylene and acetic acid process. In August 1937, Japanese interests contacted I.G. Farben for information about the Jasco acetylene process. I.G. Farben thereupon asked Standard Oil to be permitted to handle the negotiations, instead of Jasco, because I.G. Farben already has had dealing with the Japanese "and in view of the fact that I.G. have the latest experience on this subject collected in their Leuna plant." Standard Oil agreed, and thus I.G. Farben was in a position to tell the Japanese more about the process and techniques than it was revealing to its American junior partner, Standard Oil, without the latter being any the wiser of it.

While I.G. Farben pursued its research activities in Germany unhampered by its Standard Oil ties, it very definitely discouraged similar research in the U.S.A. even when it was to be done through the jointly owned Jasco.

The one-sided operation of the Jasco partnership was revealed once more to Standard Oil in 1938 when Shell was negotiating with I.G. Farben for a license to make acetic acid by a process different from that used by Jasco. Five years earlier Dr. Hochschwender had written to Standard Oil "pointing out process in question of interest to Jasco and requesting information ... to permit further study of possibilities by I.G. Farben in Germany." Despite Standard Oil's cooperation, I.G. Farben held in 1938 that the process was out of the purview of Jasco. Standard Oil protested against this view on the rather plausible ground that after helping I.G. Farben with the process, they "do not see that subsequent failure of I.G. Farben to advise Jasco of further experimentation work conducted in Germany and outlined to Shell by I.G. Farben removes process from Jasco fields." After this outburst I.G. Farben agreed to make some disclosures as to the process but it never did go to Jasco. Instead the United States patents were sold in 1940 to General Aniline and Film, then an affiliate of I.G. Farben.

In contrast to the alleged theoretical benefits which should have accrued to American companies by virtue of their foreign ties, these incidents show that in practice these advantages often did not materialize. Instead, U.S.A. research efforts were stifled and the U.S. became dangerously dependent on foreign research.

I.G. Farben also did its best to keep Standard Oil, and consequently, the United States, entirely dependent on Germany for the most modern electrical equipment required by the acetylene arc process. When Jasco was being organized in 1930, I.G. Farben agreed with a large German equipment manufacturer, Brown, Boveri & Cie., that neither would reveal the trade secrets of the other, and I.G. Farben would buy its equipment from this company. Standard Oil accepted the obligations of this agreement, thereby making Jasco completely dependent on Germany for its electrical machinery. By agreeing "not to make available to any competitor of Brown, Boveri any data or experience which, based on these tests, will be useful in the construction of an electric rectifier plant for the operation of direct current arc furnaces

in gases," Standard Oil made Jasco dependent on Germany for replacement and repair parts as well as the original installation.

On November 9, 1929, Standard and I.G. executed four separate instruments, by which the parties clothed with a constitution an alliance arrived at between them. In substance, Standard agreed to refrain from going into any chemical business in the future except as a "junior partner" of I.G. and under I.G.'s domination and control. In turn, I.G. agreed to remove itself from and stay out of the oil industry except in Germany.

Facts and details on the subject of acetic acid, the Paraflow products, the methane steam process, and the synthetic rubber patents show arresting instances of the critical impact of the 1929 agreements upon the American economy during World War II.

Indeed, I.G. Farben consistently used its power to obtain from manufacturers in other countries data on Army and Navy requirements and then, at the instigation of the German Government, played its technological controls so as to delay development of strategic materials in that country and reduce its war potential and defenses. In addition to these vicious manipulations, I.G. Farben never missed an opportunity to entrench its own dominant position at home. Thus, for instance, I.G. Farben included clauses in patent agreements precluding foreign manufacturers from supplying any technical information to anybody in Germany except I.G. Farben. Thus, I.G. Farben throttled the flow of technical information in both directions.

Part III, infra, contains typical patent contracts made by I.G. Farben which indicate to what extent I.G. Farben manipulated patents in order to gain international control over the flow of technology.

Fried. Krupp A.G.

In 1928, the German steel combine of Fried. Krupp A.G. of Essen formed in the United States a patent-holding company (Krupp Nirosta of New York). Krupp of Essen thereupon turned over to Krupp Nirosta control of all the most important patents in stainless steel field, with a proviso limiting the number of licensees, thereby limiting the production of a vital industrial and war material. In the fourteen years of its independent existence Krupp Nirosta issued only ten licenses to U.S. producers. As a further restriction measure, Krupp Nirosta refused to permit any U.S. licensee to export stainless steel except to Canada. After bringing the important foreign steel companies in as licensees, Krupp Nirosta was able to supply Krupp and the German steel industry with valuable economic intelligence. Production reports were regularly transmitted to Germany. And this U.S. subsidiary continued to transmit to Krupp of Essen (to be passed on to the Reich government) tonnage figures, including government orders, right up to the time of the outbreak of the War. In addition, Krupp representatives were permitted to visit the foreign plants freely. Krupp Nirosta also kept the Essen home

I.G. Farben has developed a special process for insulating electric conductors by using foils of polyvinylchloride covered by German Patent 736034, process for insulating electric conductors by foils of polyvinylchloride, called "Luvitherm."

A.E.G. undertakes to buy all polyvinylchloride foils needed for the process from I.G. Farben or I.G. Farben affiliates.

A.E.G. will do research work on I.G. Farben's process and improve it. For passing on its know-how to third parties A.E.G. shall be entitled to ask such third parties for a special royalty of 1 per cent calculated on the polyvinylchloride foils price paid by them. All such third parties shall be obligated by A.E.G. to purchase the needed polyvinylchloride foils from I.G. Farben or suppliers named by I.G. Farben. This license is limited to Germany.

Conclusion:

The foregoing case histories and sample contracts are typical of the uses to which German cartels put their patent rights at home and abroad. It must be apparent that this pattern will repeat, unless vigorous steps are taken to eliminate all German patent cartels, patent pools and other patent-holding abuses. Since Germany today is in possession of no exportable wealth and is relatively poor in natural resources, the only domain in which she can immediately expand to re-assert her claim to power is the technological field. Therefore, though we insist that Germany's technology be enlisted in the service of mankind, we dare not return to her control over the flow of technological information at home or abroad. Therefore, we are suggesting the inauguration of a new patent policy for Germany.

Recommendations

As presently administered, German patent law tends to prevent competition and thereby further extend the monopolization of the German economy. In the United States, for instance, it is common practice for patentees to grant non-exclusive licenses at royalties usually not in excess of 5 per cent of the sales price of the article produced under the licensed patent; whereas it has always been the German practice to exploit patents through agreements serving to divide technological fields; allocate markets and maintain a tight control over technological know-how, particularly in the electrical, chemical and other industries with a high war potential.

A New Patent Policy

Recognizing the dangers to world peace inherent in this situation, the Cartel Section of the Executive Council for Economic Foreign Policy (an inter-agency committee established by the President of the United

states to advise him on matters of foreign economic policy) started late in 1943 to consider the type of patent policy which, if instituted in Germany, would assure the elimination of those practices and would aid in firmly establishing the German economy on a free and competitive basis. Over a period of more than two years this committee diligently pursued the subject. To aid them in arriving at their final conclusions, the committee received testimony from large numbers of experts in the fields of industry, patent law and international relations. The membership of the committee included representatives from all interested Government agencies and was fortunate in having regular attendance and active participation by persons with wide industrial and patent experience such as Casper Cons, the U.S. Patent Commissioner. The final outcome of the deliberations of the committee was the patent policy for Germany set forth in a paper referred to as "ECEFP D-59" (See Appendix). This paper was presented to the President of the United States who endorsed the policy recommended therein and forwarded it to the European Theater with instructions to the Office of Military Government for Germany to consider it as the official American position as to the type of patent system which should be established in Germany by the occupying powers.

The establishment of a patent policy in Germany which will prohibit restrictive and discriminatory practices and which will prevent the abuse of patents to create protected monopolies of greater scope than the patent grant is intended to afford, is a matter of particular concern to the Decartelization Branch. It is obvious that the program of the Decartelization Branch to introduce into Germany a competitive economy would be severely handicapped by a patent law which countenanced the continuance of the type of restrictive practices which were allowed under the former German Patent Law. The Decartelization Branch is the American element of a Quadripartite Agency charged with the administration and dissolution of the former I.G. Farben industrial empire which, as the largest patent holder in Germany, owned about 18,000 patent applications and unexpired patents. Compliance with the provisions of Allied Control Council Law No. 9, which vested the I.G. Farben empire in this quadripartite body and which requires eventual complete dispersion of this property, necessitates a policy of wide utilization of the former I.G. Farben patents. If the physical facilities of the former I.G. Farben empire are to be disposed of to a large number of purchasers, it will, of course, be necessary to allow the purchaser of each unit of I.G. Farben property to utilize those I.G. Farben patents which cover the processes carried out in the purchased facilities. If the establishment of a community of interest among the purchasers of I.G. Farben units and the creation of a basis for future uniting of these interests under a gigantic patent pool is to be avoided, it is necessary that licenses under I.G. Farben patents be not restricted to purchasers of I.G. Farben facilities but also be made widely available to others.

Because of the importance to the Decartelization Program of a liberal patent policy in Germany, the

Decartelization Branch enthusiastically greeted the compulsory licensing features of the recommended future patent policy in Germany as set forth in ECEFP D-59. It is the belief of the Decartelization Branch that, if these compulsory liconsing provisions are to be successfully administered, it is necessary to clearly define the type of licenses which must be granted and the circumstances which will require their grant. Thus, it is the frequently expressed view of the Decartelization Branch that licenses should be granted only for a monetary royalty. Such a policy would discourage formation of restrictive patent pools which so often result from agreements to exchange patent licenses. To crystallize the provisions that licenses shall be granted for a reasonable royalty, it is believed that a maximum monetary royalty should be stated. It is tentatively suggested that this maximum figure might be set at 5 per cent of the retail price of the article produced under the patented process.

The Decartelization Branch is opposed to any departure from the present policy of the ECEFP as concerns the compulsory licensing of patents in Germany. The principal argument of those who advocate a change in this policy is that, to urge such a policy at this time in Quadripartite discussions would severely jeopardize the chance of obtaining Quadripartite agreement to reopen the German Patent Office. On the strength of this argument the ECEFP has agreed to restudy its patent policy as set forth in ECEFP D-59. It should be noted that whatever merit there may have been in the argument that the patent policy must be revised to assure a reopening of the Patent Office has been destroyed by recent quadripartite developments. The latest Minutes of the Legal Directorate announced that Quadripartite agreement has been reached to reopen the German Patent Office to receive applications for patents. The question of the reopening of the German Patent Office has been entirely divorced from the question of a revision of the German Patent Law. It has been agreed that the reopened German Patent Office will temporarily operate under the present German Patent Law (the 1936 revision), with only slight modifications to provide for denazification. This course was adopted as it gives more time for thorough study of sweeping reforms to the German Patent Law. The contemplated thorough reforms will be instituted, as they are agreed to, by amendments to the 1936 law. This state of facts obviously completely dispels the argument that the sweeping reforms advocated in the President's policy must be eliminated to avoid antagonizing the other powers and thus jeopardize the chances of quadripartite agreement to reopen the Patent Office.

There appears to be little concrete evidence that the recommendations for revision of the German Patent Law contained in the President's policy would be resisted by the other occupying powers as these recommendations have never been shown to the other powers. Judging from conversations of members of the Decartelization Branch with representatives of the other three occupying powers, it would appear possible that quadripartite approval of the compulsory licensing feature of the President's policy could be obtained. The Committee of Control

Officers of I.G. Farben has recently established a quadripartite Committee to study the matter of disposing of about 18,000 patents and patent applications formerly belonging to I.G. Farben. It has been the unanimous recommendation of this Committee, that the former I.G. Farben patents and patent applications be made available for licensing to all applicants. Informal discussions with the members of this Committee and with the other I.G. Farben Control Officers on the question of treatment of future German patents has indicated that they would not be averse to a compulsory patent licensing system in Germany as to all presently issued and future German patents.

It would be surprising if the Russian and British representatives did not favor a compulsory licensing program in Germany as the Russian Patent Law contains an extremely effective compulsory licensing provision and the British Patent Law contains a less effective compulsory licensing provision very similar to that now contained in German Patent Law. The compulsory licensing provisions provided in the existing German Patent Law and the British Patent Law have not been effective as they are bound around with restrictions, such as requirements for proof that a license is necessary as being in the public interest. It is worth noting in this connection, however, that the strengthening of the compulsory licensing features of the British Patent Law has recently been strongly urged by the Second Interim Report of the Departmental Committee of the Board of Trade, presented to Parliament in April 1946.

It has been argued by those who are opposed to the compulsory licensing provisions of the President's patent policy for Germany that these provisions would hinder Military Government in the accomplishment of its objectives and would interfere with the revival of permitted German industry. It is the opinion of the Decartelization Branch that a compulsory licensing provision would not only have no adverse effects upon achievement of Military Government objectives but that any other policy would be detrimental to the accomplishment of Military Government objectives. There is no possible argument that compulsory licensing of issued patents would adversely affect revival of permitted German industry. If all issued patents in Germany were made available to all manufacturers, it would go a long way toward accomplishing the necessary stimulation of competition. Such unhampered use of available technology would make possible a maximum utilization of the raw materials and productive facilities of Germany. The only possible argument that compulsory licensing would adversely affect the reconstitution of permitted German industry, would be the argument that, if the compulsory provisions were made to cover future patents, it might discourage inventors from disclosing their inventions. It is not believed by the Decartelization Branch that this argument is persuasive. Compulsory licensing at a reasonable royalty would not make patenting so unprofitable that inventors would prefer to forego patent protection and run the risk of having others learn the nature of their unprotected invention.

Although no poll has been conducted to determine whether an effective compulsory licensing program would be acceptable to the German people, the question would appear to be answered in the affirmative by the fact that German Patent Law has for many years and through many revisions had compulsory licensing features. The presence of such provisions in the statutes indicates the people's desire for such a policy even though the dictatorial administration of the policy was carried out in such manner as to make the provisions meaningless.

Indeed, the German Patent Act of 1877 contained a compulsory licensing provision (Sec. 11) which was retained through the Revisions of 1891, 1911, 1928 and 1936. The latest revision injected a certain amount of Nazi ideology into the law. Thus, the "Fuhrer" principle found expression in the requirement that permission of the Reich Cabinet ("Reichsregierung") had to be obtained before the Patent Office could act on an application for compulsory license. Action by the Cabinet was totally arbitrary, the parties involved having no opportunity to be heard, take an appeal or ask for a judicial determination. Moreover, the necessity of applying to the Reich Cabinet rendered the procedure extremely cumbersome and practically inoperative. Presently expressed wishes of German patent attorneys are to the effect that at least this Nazi amendment to the compulsory license provision (Sec. 15) be eliminated. This amendment should be removed together with the "public interest" requirement. As a practical proposition, a private applicant for license is almost always advancing a private interest and not a public one, though the latter may be served coincidentally. A realistic approach to compulsory licensing, therefore, requires elimination of the burden that a "public interest" must be proved as a condition precedent to the grant of a license.

The argument is made by some opponents to the compulsory licensing provisions of the ECEFP policy that compulsory licensing would constitute deprivation of property rights. The theory on which a patent is granted is that the Government affords a certain limited monopoly as a quid pro quo for an inventor's disclosure to the public of the method of practicing his invention. The only effect of a strenuously enforced compulsory licensing provision would be that the German Government would offer a more limited monopoly in exchange for disclosure by an inventor. The inventor would still be free to decide whether or not the consideration offered by the Government for disclosing his invention was adequate to warrant his making a disclosure.

As stated earlier, it is the present plan of the quadripartite committee on patents to immediately reopen the German Patent Office and allow the patent system in Germany to operate for the immediate future under a slightly revised version of the 1936 German Patent Law. The advantage of this plan is that it immediately fills the vacuum caused by the closing of the German Patent Office and allows the four powers more time to agree upon and institute widespread changes in the patent law. It is understood that these changes will be put into effect, as they are agreed upon, by amendments to the

1936 German Patent Law. The Decartelization Branch, in addition to strongly advocating the compulsory licensing provisions of the ECEFP policy, believes that other changes in the 1936 German Patent Law are desirable.

To aid in the enforcement of anti-cartel and anti-trust legislation, it is recommended that the 1936 Patent Law should be amended to require the registration and filing of copies of all patent license agreements in the German Patent Office. It is believed that the registration requirements should provide that failure to register an agreement will render it unenforceable in the courts and also subject the parties to fine.

The German Patent Law should be made to clearly state the principle that misuse of a patent in such a way as to create a monopoly beyond the intended scope of the patent grant will cause the patent to become unenforceable in the courts. To avoid the confusion which has arisen in the United States due to conflicting decisions as to what constitutes "a monopoly beyond the intended scope of the patent grant," those practices which will be considered as unlawful extensions of the patent monopoly should be clearly stated. Thus, specific prohibitions should be made against provisions in license agreements stipulating minimum prices, establishing a division of fields or territories, requiring licensing of future inventions, or stipulating purchase of unpatented materials from a designated source. The patent law should be further amended so as to make full disclosure of inventions mandatory. Failure to comply with such provisions should result in cancellation of the patent grant.

It would greatly facilitate the enforcement of the proposed changes in the patent law, avoid hardships to the Germans and help educate the Germans to the ways of a free economy if a system of declaratory judgments could be established to enable a prospective licensee or licensor to determine the legality of a proposed license before its execution. It is, therefore, further recommended that the German Patent Law be so amended as to provide that one or both parties may, prior to the registration of a license agreement, apply to a specially constituted patent court for a declaratory judgment as to the legality of a proposed agreement.

Summary:

In summary, it is the belief of the Decartelization Branch that the policy of compulsory licensing of German patents, as laid down by the President of the United States, should be vigorously put forward and supported as the American position; that to urge such a position would in no way jeopardize the reopening of the German Patent Office; that the principle of compulsory licensing is not unacceptable to the German people; that compulsory licensing does not constitute deprivation of property without due process of law; that the other three occupying powers would probably agree to a system of compulsory licensing; that if the avowed purposes of the occupying powers, as clearly set forth in Article III of the Potsdam Agreement providing for elimination of cartels

and excessive concentration of economic power are to be effectively carried out, an effective system of compulsory licensing is essential; that it should be required that all license agreements become a matter of public record; that specifically enumerated practices, serving to extend a patentee's monopoly beyond the scope of the patent grant, should be prohibited by statute; and that a procedure should be established by which the prospective parties to a license agreement may obtain a declaratory judgment as to its legality.

Program

In accordance with the patent policy outlined in the preceding chapters, Decartelization Branch makes the following recommendations:

1. Licenses under German patents shall be available, as a matter of right, to all applicants, on payment of a reasonable fee and without further restrictions.

2. Consideration for the grant of patent licenses shall be monetary only.

3. The amount of patent royalties shall be limited to a maximum sum of 5 per cent of the retail sales price of a patented article, a corresponding amount being fixed for licenses under process patents.

4. There shall be placed on file in the Patent Office certified complete copies of all patent licenses and other patent agreements whenever a German patent or a German national (residing in Germany), or both are involved; failure to file such copies shall make the license or agreement unenforceable and all parties thereto subject to fine.

5. Misuse of patents shall make same unenforceable. The term "misuse" shall include (without being limited thereto) the following practices: Patent cartels, patent pools; contract stipulating minimum prices; establishing division of technological fields; establishing division of territories; restricting production; setting sales quotas; requiring licensing of future inventions; stipulations as to purchase of unpatented materials from a designated source.

6. Declaratory judgment procedures shall be set up to deal with patent licenses and other patent agreements, both national and international.

7. Any party to a patent license or agreement may submit same to a declaratory judgment tribunal for approval.

8. Strict requirements for disclosure of inventions shall be enacted and enforced, so that all patents granted shall disclose the entire invention and the manner in which it is used in actual practice.

WAR DEPARTMENT
CIVIL AFFAIRS DIVISION
WASHINGTON 25, D.C.

WDSCA 072

24 September 1946

SUBJECT: U.S. Policy with Respect to German Domestic and Foreign Patents

TO : U.S. Military Governor for Germany
APO 742, % Postmaster
New York, New York

1. Inclosed is a copy of recommendations of the Executive Committee on Economic Foreign Policy with respect to German domestic and foreign patents (ECEFP D-59/46 dated 10 July 1946), together with copy of memorandum relating thereto bearing approval of the President.

2. These documents were recently transmitted by the Acting Secretary of State to the Secretary of War with the suggestion that they be forwarded to you for action.

3. Accordingly it is requested that you take such action as lies within your competence in implementation of these recommendations.

2 Incls
1. Cpy Memo to The President dtd 1 August 46 fm S/S
2. Cpy ECEFP D-59/46 dtd 10 Jul 46

O. P. ECHOLS
Major General, USA
Chief, Civil Affairs Division

DEPARTMENT OF STATE
Washington
August 1, 1946

MEMORANDUM FOR THE PRESIDENT

SUBJECT: Recommendations with Respect to German Domestic and Foreign Patents

There is enclosed herewith for your consideration a document containing policy recommendations with respect to Germany's domestic patent system and German ownership of patent rights in other countries. These recommendations, in which I concur, have been approved by the Executive Committee on Economic Foreign Policy.

The measures proposed in the document will carry out in the patent field the previously approved program to decentralize economic power in Germany and to prohibit German participation in international cartels, and will at the same time safeguard Allied security objectives.

With respect to Germany's domestic patent system, the recommendations call for immediate reopening of the German Patent Office, for making patented inventions in Germany generally available to all users at reasonable rates, and for strict enforcement of disclosure requirements. Rights in patents may be impounded or terminated by the Allied authorities. Those recommendations will require quadripartite action.

The question of German ownership of patent rights in other countries is divided into two parts--first existing patents and patent applications, and second, future patents and patent applications. With respect to existing patents this Government's policy is set forth in ECEFP D-129/45 entitled Policy of the Office of the Alien Property Custodian toward Patents of Enemy Origin which you approved on February 7, 1946 and which states, in brief, that it is the policy of the United States to make available to all nationals of the United States on a nonrestrictive, royalty-free basis the former German patent rights in this country now under direct or indirect control of the Alien Property Custodian. The present recommendations propose that this government, through appropriate channels, urge other governments to adopt a similar policy and initiate negotiations looking toward a multilateral agreement which would open up such existing German patent rights on same non-restrictive, royalty-free basis to nationals of participating governments extending reciprocity.

With respect to future German patents and patent applications in countries other than Germany, it is recommended that future inventions of German nationals resident in Germany may be patented in the United States on condition that they become the property of the United States, and that this Government issue nonexclusive, nondiscriminatory licenses at reasonable royalties to

all interested nationals of the United States and to nationals of any country pursuing a similar policy toward future German inventions. Net royalties collected by the United States Government should be transmitted to the Allied Control Authority for appropriate remuneration of the inventor in Reichsmarks. It is also recommended that the United States urge other nations to adopt the same or similar policies with respect to future German patenting outside Germany, but that this program be carried out in the United States regardless of action taken by other governments.

If you approve of these recommendations, they will be forwarded to the proper United States authorities for implementation of such portions as lie within their competence.

Dean Acheson

Enclosure
EGETP D-58/46

Approved
Harry Truman
9/17/46

ECEFP D-59/46
July 10, 1946

EXECUTIVE COMMITTEE ON ECONOMIC FOREIGN POLICY

(Report on action taken by the Executive Committee on Economic Foreign Policy on July 3, 1946)

RECOMMENDATIONS WITH RESPECT TO GERMAN DOMESTIC AND FOREIGN PATENTS

On July 3, 1946, the Executive Committee on Economic Foreign Policy considered a report from its Committee on Private Monopolies and Cartels regarding the policies which this Government should adopt and, through appropriate channels, urge other governments to adopt with respect to Germany's domestic patent system and German ownership of patent rights in other countries. The recommendations, as approved by the Executive Committee, are as follows:

I. Existing Patents and Patent Applications in Germany and Future Inventions in Germany.

The German Patent Office shall be immediately reopened as a centralized agency responsible to the Allied Control Authority and shall, in accordance with German patent law, receive applications for and grant patents on inventions made by German and foreign nationals. German patents now in effect or hereafter granted shall continue in force in accordance with the terms of the patent grants; patent applications now pending shall mature into patents in regular course. With respect to all such patents, however, the following conditions shall be maintained:

(1) Any patent now in effect or hereafter granted shall be licensed to all applicants whether or not nationals of Germany, on a nonrestrictive and nondiscriminatory basis at a reasonable royalty and for the life of the patent.

(2) In no case shall delays in the issuance of licenses be permitted to interfere with such production, use, sale, or importation as the occupation authorities may deem desirable.

(3) Existing provisions of German statutes, supplemented if necessary, requiring disclosure of sufficient information to render the invention claimed in the patent capable of practical exploitation shall be strictly enforced. Initial absence of such disclosure or failure promptly to correct insufficiency of disclosure shall be ground for invalidation of the patent, provided, however, that technical information, whether or not protected by patents, shall not be published if the occupation authorities deem publication prejudicial to security.

(4) The occupation authorities shall take such steps, including necessary revisions of the German patent laws, to prohibit permanently the German Patent Office from maintaining a class of secret patents except as ordered in specific cases for the benefit of the occupation authorities.

(5) Rights in patents and patent contracts and rights to the issuance of patents shall be subject to such blocking, impounding, security and other measures as the Allied authorities may prescribe. Such measures may include dedication to the public by termination, if it is decided that such termination will further any program which may be adopted by the occupation authorities concerning the disestablishment of combines, cartels or other prohibited arrangements.

II. German Ownership of Patent Rights in Countries other than Germany.

A. Existing patents and patent applications.

(1) It shall be the policy of the United States to urge upon other interested governments that every vestige of German ownership or interest in existing patents and patent applications in countries other than Germany should be terminated, and that jurisdictional questions of authority or questions of the ultimate disposition of such patents should not be permitted to impede prompt termination of the German interest.

(2) It is the policy of the United States to make available to all nationals of the United States on a nonrestrictive and royalty-free basis the former German patent rights in this country now under direct or indirect control of the Alien Property Custodian. The principles and qualifications of this policy are set forth in ECEFP D-129/45 of October 3, 1945, entitled Policy of the Office of the Alien Property Custodian toward Patents of Enemy Origin.

(3) Diplomatic action shall be undertaken to arrive at a multilateral agreement among the various United Nations and neutral governments whereby German-owned or controlled patent rights, or patent rights owned or controlled directly or indirectly by the Alien Property Custodians or similar officers and agencies of the signatory governments, would be opened, subject to appropriate qualifications, on a nonrestrictive and royalty-free basis to all nationals of participating governments extending reciprocity.

(4) The policy of opening up these patent rights on this basis to the fullest extent possible is also recommended as an objective to be sought in countries other than those included in (3).

(5) No German-owned patent or patent application, the German interest in which has been eliminated pursuant to the policies herein indorsed, shall be used to bar the import of German commodities into the United States whenever the Allied Control Authority or the United States Military Governor determines that shipments of such commodities from Germany are appropriate, and in such cases the United States shall license the importer under the patent on the same terms as United States nationals are licensed. The United States shall recommend to other nations the adoption of a similar policy.

B. Future patents and patent applications.

(1) No patent shall issue in any jurisdiction other than Germany on any invention (a) made in Germany or other enemy territory by a German national during the period September 3, 1939 to December 31, 1945, or (b) made in any formerly enemy-occupied territory by a German national from the date of initial occupation of that territory to December 31, 1945; except that patent applications already filed in jurisdiction other than Germany on such inventions may issue to patent, and such patents shall then be treated in accord with the recommendations in II.A. of this paper.

(2) Inventions made in Germany subsequent to December 31, 1945, during the period of Allied occupation or control and any additional period which may later be provided, shall be available for use in countries other than Germany on a nonrestrictive, nondiscriminatory, nonexclusive basis at reasonable royalties.

(3) To provide for such use in the United States, any inventor in Germany, other than an undesirable person as defined by the denazification law or other occupation regulations, shall be permitted to file applications with the United States Patent Office on such inventions, on the condition that any patent issued upon such application shall become property of the United States. The inventor shall execute any documents and perform any acts necessary to effectuate this purpose. The United States Government shall provide for the issuance of non-restrictive and nondiscriminatory licenses under any such patent at a reasonable royalty and for the life of the patent, to all nationals of the United States and of reciprocating foreign countries. Royalty rates shall be determined in the sole discretion of the United States Government; and any royalties collected by the United States Government shall be transmitted, after deduction of administrative expenses, to the Allied Control Authority, which shall make appropriate provision for remunerating the inventor in Reichsmarks.

(4) Subject to consideration of national security and of administrative desirability, the United States shall publish, as soon as practicable after application, the specifications contained in patent applications filed pursuant to (3).

(5) No patent issued pursuant to (3) shall be used to bar the import of German commodities into the United States whenever the Allied Control Authority determines that shipments of such commodities from Germany are appropriate. In such cases, the United States shall license the importer under the patent on the same terms as United States nationals are licensed.

(6) The United States shall recommend to the governments of other nations the adoption of the policies specified in (1), (2), (3), (4), and (5) or of policies as similar as practicable in view of their legal systems.

(7) The United States shall take reasonable steps to make the German know-how available to all licensees under any patent issued pursuant to (3).

(8) The United States shall adopt, and shall recommend general adoption of the principle that no German national in Germany shall be permitted, during the period of Allied occupation or control and any additional period which may later be provided, to acquire any rights other than a nonexclusive, right of use, in inventions or technical information existing in any country other than Germany or in patents issued or patent applications filed in such country.

RECOMMENDATIONS

Introduction

The problem of decentralizing the control of the German Economy outlawing cartel practices and restoring a freely competing market might be regarded as a very limited and special problem to be isolated and attacked in fairly simple fashion, apart from the main stream of German economics. However, to treat any basic economic problem without reference to the medium in which it operates is not only shortsighted but misleading. To treat one of the broadest and most nearly all-inclusive problems in the German economic field in such a fashion would be even more: it would be foolhardy and dangerous.

The solution of the cartel-deconcentration problem is of particular importance to Germany. Germany has been called the cradle of cartels; a nursery of restrictive practices and a school for monopoly. As late as 1780, on the eve of the French Revolution, feudalism was still relatively strong in Germany, firmly based economically, ruthless, and a source of misery to the masses of the people. During the last phases of feudalism, there was increasing state regulation in support of the ruling classes, few in number and grown too weak to defend themselves against the growing power of the merchants and industrialists. Monopolies, directed against the interests of the people, are a phenomenon often observed in a moribund society, whether it be called feudalism, imperialism or national socialism. In Germany these monopolies were often localized, conferring exclusive rights to certain towns or cities or states, or to certain families, guilds or manufacturing establishments. Under Bismarck, they took the form of cartels and combines used to exercise complete control over whole segments of the economic system, including international trade. Cartels and increasingly concentrated enterprises also used their close connections with government to influence and gain favors from the state.

Yet speakers and writers now frequently refer to Germany, its politics and economics, as if it were a vacuum into which the Allied occupying forces entered after Germany surrendered in May 1945. Nothing could be further from the truth, despite evidence of widespread destruction and devastation. From the standpoint of economic concentration Germany, at the time of its second defeat in twenty-five years, was dominated by closely controlled economic concerns engaged in monopolistic and restrictive trade practices. Bribery was everywhere resorted to; economic relations were close, well-defined, almost crystallized. While the forms and superficial aspects of a democratic system may have received lip service, basically Germany had reverted to economic feudalism. Nor was this result a surprise to those who had followed the history and development of the German cartel system. It might even be said that manpower, factories, patents, inventions, property, houses, were all regarded as pawns in the game being played by coal and steel barons, corporate kings, aircraft generals, and an occasional house painter and champagne salesman.

Among the many devices and practices contributing to the development and support of this "throwback" system were: the widespread use of the cartel device; the close regulation and

direction of foreign trade by means of tariffs, multiple currencies and other unduly numerous; the delegation of governmental powers to self-constituted private groups such as trade associations and chambers of commerce; the organization of special economic chambers and rings; the encouragement and fostering of the development of excessive economic concentrations by sponsoring the widespread practice of interlocking directorships and officerships and proxy voting; limiting the rights of shareholders as compared to the power of the Vorstand and Aufsichtsrat; the approval of private pricing systems; legalizing the use of bearer securities so that the detail of ownership patterns could not be determined; the delegation of power to allocate scarce materials, either to private groups or in accordance with the wishes of private groups; the setting up of compulsory and exclusive arbitration procedures outside of the court system which aided in preventing individual action by small and mediumsized business firms to protect their rights under the laws; emphasis upon the use of the holding company device; encouraging the development of the family complex; converting and modifying the practices of cooperative organizations to form powerful combines under deceptive labels. Banks and financial institutions played a decisive role, financing armaments production, consolidating controls, concealing ownership patterns, and bolstering the weaknesses of rushroomed corporate structures. The power of taxation was used to discriminate against small and medium-sized concerns. This closely integrated, tightly held economy, disguised as "socialism" was in fact the "vacuum" into which the military government moved when they marched into the demolished or battered cities of Germany. These deep-rooted manifestations of the real German system, the age-long expression of German philosophy and German ideals, cannot be uprooted overnight. They will not wither in the light of occupation. They cannot be erased with democratic phrases or by simply allowing the Germans to vote. German business ethics and practices must be re-formed and placed on a higher level than ever before in Germany. Discrimination, bribery, nepotism, unfair trade practices, cartels, combines or special privileges must be made "reprehensible", and not allowed to remain in the German conscience as "clever" words. Honesty, fairplay, individualism, etc. must become respected and sought-after words. While time is of the essence, time is available. Major steps can be taken now for the reorganization of Germany on a peaceful basis. The entire German economy can be reorganized during the next few years if we have a will to do it.

There undoubtedly are many approaches to this problem. All of them will have much in common. All of them will involve a great many minor or supplementary steps and objectives. Many of the basic approaches to the peaceful reorientation of the German economy will include the same over-all objectives. Nearly all of them will include as a major objective the elimination of excessive concentrations of economic power in Germany as exemplified in particular by cartels, syndicates, trusts and other monopolistic arrangements. However, the elimination of cartels, syndicates, trusts and other monopolistic arrangements will not of itself do more than aid in a temporary and fairly superficial solution of the problem. Many other basic steps must be taken both as an aid in the reorganization of the German economy and as a bulwark in support of such a reorganized, democratic economy. A number of these supplementary and complementary steps are described in the following pages. These sug-

gestions are offered, not as an absolute program, but simply as some of the guide posts and trail markers which should be considered in any economic revival of Germany. It should be remembered that what is being attempted is simply to define the problems, indicate possible solutions to some of them, and suggest that Germany adopt accepted basic world-wide ethical standards for its economic conduct. There is no intention to argue that the economic system as it is found in the United States should be exported to Germany. There is in the alternative, however, no disposition to accept the idea so prevalent in certain circles that the economic experience of the United States has no validity anywhere else. German business conduct must be improved. The following suggestions are standards which could be used.

Holding Companies

Problem

Ownership or control of one company by another through the device of stock ownership is widely practiced in Germany. This practice has developed in some instances to the extent that billions of Reichsmark worth of property have been combined under a single management. Actually, the holding company device simply superimposes one legal fiction upon another legal fiction. Control is gained through the voting of stock without necessitating the actual close integration into one firm of the assets of the subject corporations. Great control can be exercised by one company over another by the investement of a relatively small amount of capital. This is particularly true where multiple voting shares, less than 100 per cent paid stock, and other similar devices are used. The financial technique of placing voting control into the hands of only common stockholders, or even certain special types of common stockholders, while the bondholders and preferred stockholders have no voting rights, facilitates the pyramiding of the control of large numbers of corporations, both vertically and horizontally. Often such companies are related to each other only through such financial manipulation of the stock ownership; i.e., there are no operating relations between the companies themselves. The holding company device also facilitates the flow of profits from operating companies to a central parent company or companies in such a manner as to give exceptionally great dividend preference to certain stockholders vis-a-vis the stockholders of other companies in the complex, particularly operating companies. Holding companies may have subsidiaries through the 4th, 5th, 6th or even more generations. Some of such units may be held by several other subsidiary units. Some of the ownership pattern may be concealed by being held under false names, dummies, banks acting in a confidential relationship, and similar practices. The control also often carries with it the fixing of all policies of all the subsidary corporations, including labor, social, dividend and selection of products.

The holding company device is essentially, when carried to an extreme, an unstable economic arrangement. Often if some part of the holding company fails the entire structure will fail despite the fact that certain units of it are entirely sound. Even if the sound units do not also fail, they will

often be subjected to substantial financial loss.

Recommendation

That ownership of one company by another be limited in any event to the second or third generation, with proper provisions for a small number of limited exceptions mentioned below. In the case of combines found to have engaged in restrictive practices or otherwise to constitute excessive concentrations of economic power, the limitation upon stockholding by one company in another should be substantially prohibitive.

Discussion

The limiting of the holding company structure to the second or third generation would force to a major extent the simplification of a large part of the corporate structure of the German economy. It would aid in limiting the holding of one company's stock by another except where there is an economic reason for it. This recommendation probably should provide, however, for certain limited exceptions. One possible modification might be to allow a greater number of generations of ownership of subsidiaries so long as such ownership beyond the second or third generation was at least 95 per cent. Certain flexibility in arranging its corporate structure could thus be provided for. This would allow a corporation to organize extra subsidiaries to enter a new field and to take certain risks which the parent company might not feel desirable at a given time. It would allow the incorporation of extra subsidiaries in order to comply with various local conditions. This type of exception should be carefully weighed, however, against the disadvantages of corporate complexity.

The owning of stock to a degree less than 5 per cent in any company might also be allowed as long as such holding was not the first, second or third (or more?) greatest holding of stock in such corporation. This would allow legitimate investment of corporate funds but would not allow the control of another corporation if the exception were properly restricted.

A corporation might also be enabled to hold between 5 per cent and 95 per cent of the stock of another corporation for periods less than a year (as long as it was not voted) for various reasons; among them, that the ownership of such stock was obtained through default or because an attempt was being made to buy the legal control of another corporation, which control could not be obtained in a relatively short period of time.

The simplification of corporate structure in Germany would, of course, lead to easier supervision and control of the German economy by either Military Government or any future German government. It would aid in preventing the concealment of assets, and similar practices. None of the above exceptions should be permitted in connection with the compulsory reorganization of combines which have been found to violate the laws prohibiting excessive concentration of economic power.

The holding company may combine competitors, thereby preventing competition. It may gain such a dominant position in the market as to exert unreasonable control of the market, ultimately becoming a monopoly. The above recommendations taken as

a whole should limit the use of holding company relationships to legitimate objectives and aid in preventing their use for purposes inconsistent with decartelization objectives.

Family Complexes

Problem

The development of huge concentrations of economic power through the accumulation of holdings into the hands of members of a single family is not a peculiarly German development, though it has reached in Germany a very advanced stage. Perhaps the only place in the world where the family complex device has been developed to a greater extent is in Japan where the overwhelming control of the economy was exercised through the use of 5 or 6 private and basically family enterprises called "Zaibatsu". The family method of concentrating economic controls usually entails the use of a number of other devices, including elaborate holding companies, huge combines, control of banks, which in turn control credit policies, interlocking directorships and officerships, and cartel agreements. The basic agreements among the members of the family itself can be readily concealed, are often oral, and are compelling on each member by virtue of the fact of his family relationship. The economic complex is often linked by marriage with native militarists and members of the armed forces, politically prominent persons, or other powerful individuals. It is by means of the combination of (a) western capitalistic methods such as the use of stock corporations, holding companies, and similar devices, and (b) the feudalistic family complex, that some of the most restrictive monopolies and largest concentrations of economic power in present day economic history have been formed. It is by the use of the family complex device that great financial interrelation of what would be otherwise technically independent enterprises, is obtained.

Recommendation

That for purposes of deconcentration family holdings be considered as mutually inter-dependent until it is proven beyond question that such holdings are in fact independent.

Discussion

The organization of the German family complex, an organization fostered by educational and sociological orientation, is feudal in character. The family head exercises almost absolute authority and his word is not often subject to contravention. Despite the fact that holdings by various members of a family are nominally independent, the force for unified and concerted action resulting from the family relationship is frequently as strong as if legal community of interest existed. Since the purpose of the decartelization and deconcentration policy is to abolish economic concentration in Germany, family complexes should be carefully examined, regardless of the apparent financial independence of the components, to assure that they are not, in fact, operating in restrictive way. Among others, families which will have to

be specially studied are the following: Haniel, Krupp, Flick, Stinnes, Quandt, Henschel, and Bosch, in addition to other secondary family groups which have permeated combines such as I.G. Farben, which was principally held together by other means.

Control by Banks and Financial Institutions

Problem

It has been estimated that the big six banks of Germany - Deutsche Bank, Dresdener Bank, Commerz Bank, Berliner-Handels-gesellschaft, Bank der Deutschen Arbeit, and Reichs-Kredit Gesellschaft - voted over 70 per cent of the voting stock of the major industrial enterprises in Germany. These banks were themselves indirectly related by having their officers and directors act as officers and directors in common on other credit institutions, industrial and commercial enterprises. They also were related by marriage and through membership in varied social clubs and by other social activities. The controls they exercised were both direct - through stock ownership, through directorships and officerships of other corporations - and indirect, through flotation of stock and bond issues, stock exchange operations, granting of credit on extremely limited conditions, through "friendly advice" and through social and family relationships. Proxy voting and nepotism were favorite devices.

Recommendation

That common stock ownership and voting by financial institutions be eliminated, interlocking directorships and officerships between financial institutions and business enterprises severely curtailed, investment functions separated from banking functions, and the extension of credit and the giving of advice on conditions tantamount to control of an enterprise be prohibited.

Discussion

In Germany the practice of bank voting of common stock was the rule rather than the exception. The normal investor in Germany deposited his stock with his banker who collected dividends and credited them to the owner's account and voted it in the majority of cases. Proxies were freely given, for periods normally up to 15 months. Banks extended credit on conditions limiting the purposes for which the money could be used tantamount (in many cases to running the company), or on condition that a member of the bank became a member of the board of directors of the debtor, or on condition that the bank be allowed to influence the voting of a certain amount of the corporation's stock until the loan was repaid. Debtors often found it difficult to remove these "temporary" directors and influences.

At a very minimum, the practice of interlocking officerships and directorships should be prohibited where there is any fiduciary relationship between the companies in question, where they are competitors in the same or similar fields or where such interlocking relates corporations whose total em-

ployment exceeds a certain size. The directorships or officerships which a single individual can hold should be further curtailed (a slight curtailment exists in German law today), and be limited to a relatively few in number if more than one. The above principles, if carried out, would be particularly effective in breaking the control of the economy of Germany into the hands of many independent businessmen throughout Germany. It would also result in placing the responsibility of making economic decisions into the hands of those men of business, thereby accomplishing a substantial decentralization and deconcentration of economic power.

Interlocking Directorships and Officerships

Problem

Thousands of German economic enterprises are closely interrelated through the use of common directors and common officers. Thereby policies in one organization are directly transmitted or conditioned by the policies of another. Concerted action to dominate or control a market is facilitated and encouraged. Monopoly effects may be obtained if the interlocking combines control a sufficiently large proportion of the available facilities in the field in question. The interlocking in unrelated fields combines monopolies and facilitates concentration of tremendous economic power into the hands of a few manipulators. While German law does limit this practice to some extent, such limitations are so minor that their prohibitions are rarely felt.

Recommendation

That the practice of using common directors and officers be prohibited or curtailed by law to the extent necessary to eliminate the above-stated abuses; and specifically that in the case of all companies which are found to be objectionable in their structure or practices, their principal officers and directors be required to select the one office or directorship which they wish to retain, and relinquish all other major offices and directorships.

Discussion

At a very minimum, the practice of interlocking officerships and directorships should be curtailed to prevent any interlocking where there is any fiduciary relationship between the companies in question, where the companies could in any way be considered as competitors in the same field or line of commerce, or where such interlocking relates corporations whose total employment exceeds a certain size. The use of common directors and officers has become extremely widespread in Germany. Through the use of interlocking directors and officers the combined weight of several enterprises can be brought to bear on a given subject. The subject may be prices, territorial allotments, production quotas, a competitor, etc. The total power of these combined groups may become much greater than the arithmetical total of the single power of each. The interlocking device aids in preventing economic decisions from being made by many individuals in society at large, centering such decisions in the hands of a few men or concerns. Preventing certain

directorates and officerships from existing will aid in returning to the hands of thousands of businessmen the right to make economic decisions which are now denied to many and usurped by the few. The elimination of concerted action by purportedly independent units will thus aid in eliminating existing and preventing the formation of future cartels and excessive concentrations of German economic power.

Restoration of Stockholders' Rights and Responsibilities

Problem

As a result of laws and decrees promulgated under the Third Reich, the corporate entity was identified with its managerial boards, and stockholders were divested of all important control over corporate activities or policies. The most important and effective step in this regard was the issuance of the German Corporation Act of 1937 (Gesetz ueber Aktiengesellschaften und Kommanditgesellschaften auf Aktien § Aktiengesetz §). This act provided in part:

§ 125. Establishing the Annual Financial Report (Feststellung des Jahresabschlusses).

(1) Within three months following the preceding fiscal year, the board of directors shall prepare the balance sheet statement and the profit and loss account (final accounting for the year) and present the same to the supervisory committee. The articles of incorporation may provide for not more than five months within which this may be done.

(2) The supervisory committee has one month within which to examine the financial accounts presented by the board of directors.

(3) Where the supervisory committee approves the financial accounts they are regarded as established provided that neither the board of directors nor the supervisory committee submit the accounts to the general meeting.

Recommendation

In line with the other recommendations contained in this report, it is felt that the German Corporation Law must be amended to provide: (a) that the final accounting of the board of directors for each fiscal year must be submitted to, and must be approved at the general meeting of the stockholders; (b) that each stockholder must have free access to the books and ledgers of the corporation; (c) that each stockholder must be given the right to prosecute an action in the courts, on behalf of the corporation, and against the directors, officers, managers or other agents, whenever managerial action is being taken to the prejudice of the corporation, through either misfeasance, malfeasance, or non-feasance. This right of action should include the right to bring action to compel the declaration

and distribution of dividends where examination of the corporate books indicates that such action is proper.

Discussion

The German Corporation Act of 1937 effectively introduced the concept of the Fuehrer Principle into the structure of domestic German corporations. The act redefined the relationship of stockholders to the corporation, taking away from them all right or power to control the corporate activities, at the same time strengthening the position of the board of directors against what the Academy of German Law characterized "the mass of irresponsible shareholders who largely lack the necessary insight into the position of business". This concentration of power in the board of directors, who were both de facto and de jure independent of the stockholders, when coupled with the maze of interlocking directorates which permeated the German industrial system, facilitated the formation of monopolistic combines, and the authoritarian regimentation of German industry.

By restoring ultimate control of the corporation to the individual stockholders, and by giving to them the remedy of the "stockholders' representative action" German industry would be made more responsive to democratic forms of control since all managerial acts would be subject to review and recall both at stockholders' meetings, and in the courts.

Registration of Security Issues

Problem

Intelligent regulation of a securities market requires knowledge on the part of the government of certain basic facts in regard to the plan of issuing the stock and basic data regarding the capital structure of the corporation. The establishment of a peaceful German economy requires the development of a sound investment and security market. Knowledge of certain basic facts in regard to all stock issues and basic data regarding the capital structure of corporations is vitally necessary to the intelligent purchase of stock by persons outside of the corporation. Requiring the filing of the basic and essential facts regarding a corporation and its contemplated stock issue aids in preventing fraudulent issue from being successful and also aids in building public confidence in stock transactions and in stock exchanges and in the making small savings available for investment along democratic lines. The purchase and sale of corporate stock is essential to enable small investors to own a part of the productive facilities of their economy. It also is a device whereby the ownership and responsibility of managing large amounts of capital can be divided among a large group of people, thus aiding in placing the right to make economic decisions into the hands of many rather than a few persons. The stock device, of course, can be used for concentrating the control of a large amount of economic power in the hands of a few people. However, the placing on public record the entire control and factual situation of a corporation, as well as a statement of its actual functions and value, will aid in preventing fraudulent practices of many kinds. Such steps will also be of aid in the formation of and the continu-

[illegible] of an economic democracy where an open and free market for goods, services, securities, etc. is dependent upon the [illegible] the shocks of technological obsolescence, changes in supply and demand, adjustments due to changes in investment policies, etc.

Recommendation

That existing German corporation and commercial [illegible] exchange legislation be amended to provide for a full disclosure of facts relevant to all types of security issues and that such information be made more easily accessible to the public at large (and possibly that this information be recorded at a central German office, particularly in regard to concerns exceeding a certain size).

Discussion

To effect the above recommendation, a registration of securities should include a number of basic requirements: (some of these are already required under German law).

1. A detailed balance sheet with a profit and loss statement for the latest fiscal year and each of the two previous years plus a schedule of underlying facts.

2. A statement of the capital stock and funded indebtedness before and after issue of the new securities, terms of such securities, etc.

3. It should include a statement of purposes for which the resultant money will be used and, in case there are several purposes, the amounts devoted and an explanation as to each.

4. A schedule should be given, setting forth the salaries, bonuses and other remunerations of officers and directors receiving more than RM 25,000 per year.

5. A complete account of the expenses involved in the floating of the issue should be stated.

6. If any stock is to be transferred at less than market price, or if any person is to receive a special deal in advance of public issue, such information should be carefully stated and explained.

7. Copies of all documents such as articles of incorporation, major agreements including underwriting agreements, contracts for special bonuses, etc. should be fully set out.

Other requirements also of considerable importance in the guaranteeing of a stable and honest security market might include compelling corporation officials to file each month all holdings of stock in their own corporation over 10 per cent of the total amount of such stock issued, or if such holding was among the 10 or 12 largest stockholdings of the company. The registration might also require turning over all profits made from the sale of any corporate stock held by any official in

his own corporation, if such stock was held less than six months.

The solicitation of proxies should be in accordance with special rules and stock traders and stock brokers should not be allowed to solicit proxies of or vote stock held on account. The law should include both civil and criminal penalties and probably should also contain certain exceptions as to the registration of local or foreign government bonds or securities of an enterprise which is otherwise sufficiently controlled by a government so that registration would be deemed to be unnecessary. Securities maturing in less than 9 months or some such period of time, non-profit and charitable institutions below some figure such as RM 100,000, could also be exempted.

The problem of standardized evaluation procedures becomes of real importance where an attempt is made to expose by registration the real worth of a corporation. Because of the extensive war damage suffered in Germany, companies which are reorganized and which offer new issues of stock might well be required to use a standard formula based on present replacement value. Continued amortization of war losses would be checked thereby. To assist Military Government in its surveillance of the German economy, it would also be of value to insist that the registration statement be filed in English and make the English filing the official statement. Accounting methods now used should be screened to determine whether they should be modified and further standardized. Such a standardized system would facilitate both German and Military Government supervision.

The above suggested requirements need not be particularly complex and one initiated would require a company to organize its accounting practice so that all of the pertinent data would be available automatically at any stated period of time. No great burden would thus be placed on a concern.

Bearer Securities

Problem

Germany prior to the war followed the practice of using bearer shares to an unprecedented degree. Such shares are not registered in the name of any person or persons and can be freely passed from holder to holder. Each holder is prima facie the owner of the security and therefore has full right of voting the stock during the time of holding such securities. Bearer shares represent in Germany a second medium of exchange - in effect a substitute money. They have been used and are being used as a device for concealing the actual ownership of economic enterprises because only at occasional stockholders meetingsdoes it become necessary to reveal any evidence of the ownership of the enterprise. Such revelation is rarely accurate or conclusive.

Investigation to uncover evidence of concentrations of control is hampered because of the lack of ownership records. Records of dividend payments, which might ordinarily serve as evidence of beneficial ownership, are obscured by the fact that dividends are paid into a common pool at a bank without break-

down. Because bearer shares so often find their way into a central depository, the Big Six banks of Germany, non-owners and merely holders of bearer shares, have been enabled to exercise voting control over an overwhelming portion of the major economic enterprises in Germany.

Recommendation

It is recommended that the issue and use of bearer shares be prohibited and that all certificates of ownership of German economic enterprises be converted into registered securities showing both the legal and beneficial ownership.

Discussion

Carrying out the above recommendation will (1) help to place upon the actual owners of economic enterprises the responsibility for the control of such enterprises, (2) reveal to German and Military Governments the ownership patterns of the various units of the German economy so that intelligent and enlightened regulation can take place, and (3) aid in decreasing the concentration of economic power in Germany. Individual stock owners will be enabled to determine with whom they are associated in ownership of economic enterprises; will be aided in their formation of minority stockholders group if that is their desire; and will in the long run be required to exercise more responsibility in the management of the enterprise which they own than has been the case heretofore.

Proxy Voting

Problem

The apathy of small stockholders towards the voting of stock has been very pronounced in Germany and probably is impossible of complete solution. The powers of the Vorstand and the Aufsichtsrat have been expanded by law, vis-a-vis the stockholder. Another cause for such stockholder apathy is a feeling that there is no use voting when the majority stock interest is so easily controlled by a certain few stockholders and the management of the enterprise. This apathy is also caused in some degree because the small stockholder finds it difficult to form minority groups for the reason that proxies have already been given out by other stockholders for long periods of time.

It has been estimated that as high as 70 per cent of the shares of the major industrial and commercial enterprises in Germany have been deposited with banks in Berlin. The right to vote the shares so deposited usually also has been relinquished by the owners of such shares to such banks who have centralized their security deposits. This practice of depositing shares in banks has concentrated into the hands of a few related banks an enormous amount of control over the entire German economy.

Recommendation

That proxy grants by owners of securities be limited to a relatively short period of time, possibly not longer than a single meeting or a group of closely related meetings, that the power of banks to vote stocks or shares be eliminated, and that it be required that proxy forms be submitted to all stockholders. Stock traders and brokers should not be allowed to solicit proxies of or vote stock held on account.

Discussion

So that stockholders will be more completely informed as to the purposes to which their proxies will be put, it is recommended, also, that the proxy form contain a statement of the questions to be voted. The management should, therefore, be charged with the preparation and circulation of a complete agenda.

The above recommendation does not solve the problem of self-perpetuating management, nor is it intended to do so. It is directed, however, at making it necessary for stockholders to grant their proxy powers more often and thus compel them at least to reconsider the matter at certain frequent intervals. It would also prevent proxies from being given for a long period of time, which tends to preclude the giver from being able to change the grant of his proxy power at will. This recommendation will thus aid in increasing the flexibility of, and make it easier for a shareholder to exercise the authority which is his by virtue of ownership of securities. It will also aid in making management more responsive to shareholders and thus aid in the elimination and prevention of the maintenance of excessive concentrations of economic power.

Cooperatives

Problem

The cooperative movement developed in Germany at a very early period. Many of the basic principles used in the formation of cooperatives in the rest of the world were also adopted at an early date by the German cooperative movement. During the period of time that the Nazis were in power, however, the German cooperative law was altered to a major extent. In fact, many of the basic principles were substantially modified, some of them beyond recognition. The cooperative method of organization, properly limited, can be used as a democratic instrument for obtaining ends not easily obtained by the use of the corporation, partnership or other organizational device. Cooperative principles can, of course, be abused and cooperatives can be organized ostensibly as cooperatives but actually as means to conceal cartel practices. If basic principles are adhered to, however, the cooperative method offers an efficient and justifiable means for a limited form of joint action.

Recommendations

That cooperatives be authorized, but that their activity be strictly limited by the following principles:

a) membership to be voluntary and open to all who wish to join, without distinction of race or creed (political and religious neutrality to be maintained);

b) admission to membership and to official position in a cooperative or cooperative association to be governed by the Law for Liberation from National Socialism and Militarism of 5 March 1946;

c) the controlling administrative elements of the cooperative to be elected in accordance with democratic principles;

d) in all voting each member of a cooperative to have one vote and not more than one vote;

e) earnings to be distributed among members in proportion to their participation in the business of the cooperative; and

f) rates of interest on voluntary investments of members, as distinct from rebates on purchases, to be limited.

Discussion

Cooperatives may be consumer cooperatives or producer cooperatives. They may also represent combinations or variations of these. Consumer cooperatives are usually organized to enable an already closely related group to purchase in large quantities, or to purchase particular items. Producer cooperatives are also organized to enable the members to take joint action. This latter type of cooperative, however, may very well attempt to monopolize a given industry or to discriminate among consumers in certain ways or engage in other practices which would be inconsistent with a decartelization program. If, however, cooperative practices are subject to the same standards of business conduct that are applied to other economic enterprises and they live up to the stated principles, their organization and functioning can be justified.

Trade Associations and Chambers of Commerce

Problem

Privately organized trade associations and chambers of commerce have been more widely used perhaps in Germany than in any other country as a mean of centralized control. During the Nazi period they were particularly stressed, became a part of the governmental control machinery, and were relied on to police and exercise absolute control over nearly every important market in Germany. Even before the Nazis, however, trade associations and chambers of commerce exercised tremen-

dous influence over all phases of the German economy, especially production, distribution and sale.

Trade associations in Germany are normally limited to a single industrial field while chambers of commerce normally combine local industrial units in several fields. Thus complete vertical and horizontal integration of an economy can be achieved by the use of trade associations and chambers of commerce, and was so achieved in Germany. Trade associations in Germany became completely monopolistic organizations controlling, in an overwhelming number of cases, 100 per cent of the industry from which they were organized. Trade associations fixed prices, collaborated on general business rules, prohibited new investment, eliminated what they defined to be "unfair competition", compelled the furnishing of certain information by each member, such as pricing and cost data, organized exclusive and compulsory arbitration procedures and appointed the members thereof, and otherwise restricted and controlled the action of the members through what amounted to a privately operated government.

Chambers of commerce brought various pressures to bear on their members to compel them to live up to the chambers' own interpretation of "fair practices". They acted as a coordinating medium between members of the various trade associations and increased both their own and the power of the trade associations. This was particularly true of national chambers and associations. Chambers of commerce in Germany have been delegated the power to allocate scarce materials which gave them, of course, the power of life or death over participant enterprises. Chambers of commerce exerted influence on local and national legislation in such a way as to support the restrictive practices and preserve the status quo of the various chambers of commerce and trade associations. Local chambers of commerce had a great influence in the social life of the locality and exerted great power in the direction of complete conformity to their standards.

Recommendation

That the membership of any chamber of commerce or trade association be limited to a single Land, that they be prohibited from exercising government functions or responsibilities, and that they be prohibited from using or participating in exclusive and compulsory arbitration procedures or acting in any concerted fashion to compel a member to comply with regulations inconsistent with decartelization principles.

Discussion

Trade associations and chambers of commerce should not be permitted to place discriminatory restrictions on membership. They should not be allowed to exercise any authority or control over or to participate in distribution, sales, marketing, pricing, allocation of orders, materials or fuels, licensing of business, setting of production quotas, etc. in the field or fields in which they operate or in any other field. They should not engage in business, and their primary function should be to act in an advisory capacity both to their own members and to any other organization which desires or might benefit from such advice. Chambers of commerce and

trade associations should be required to make public their by-laws and principles of operation and especially close supervision should be maintained over their functions and actions for a considerable time in the future to ensure that they do not again abuse their position in the German economy.

Arbitration

Problem

German enterprises, trade associations and chambers of commerce developed to a very high degree in Germany the practice of using compulsory and exclusive arbitration procedures for the private adjustment of conflicts of all kinds. Arbitration procedures were used to settle disputes relating to such matters as quotas, prices and allocation of raw materials. Often acceptance of the arbitration provision was made a condition on admittance to an association or chamber of commerce, and was provided for in a large number of standard contract forms. These arbitration procedures often, and probably usually, compelled the parties to the agreement to arbitrate under privately established rules and excluded appeal from such proceedings to regularly constituted judicial courts. Often the third member of an arbitration board would be picked by the president of a local chamber of commerce or some other organization which would be primarily interested in maintaining the status quo and preventing any competitive initiative being shown on the part of an individual. The terms of the arbitration proceedings could and in a very substantial number of cases did favor the most powerful party to the agreement.

Recommendation

That the practice of using compulsory arbitration procedures to the exclusion of normal remedies at law be prohibited in Germany.

Discussion

The principle of arbitration is a valid one when not used to excess. On the other hand one of the basic elements that modern society has devised for protection of the individual is the independent judiciary. To preclude an individual from taking his disputes to such an independently established and independently acting body is to place him in a poor bargaining position vis-a-vis those who enforce this requirement. As society grows more and more complex, it becomes increasingly necessary to insist that the procedures whereby an individual can protect himself from the possible arbitrary action of his fellow man must not be taken from him, and that he should not be allowed to contract them away.

Arbitration is only justifiable if it is entered into on a voluntary basis on the part of the participants. The agreeing to arbitration procedures for long periods of time and in respect to a complete range of subject matters, in order to gain membership in an organization or in order to obtain a contract for the supply of materials, circumscribes an indivi-

dual's freedom to act to an extent that it can become a weapon in the hands of the controlling groups which is in a position to require such acceptance. If, as a matter of law, it is not possible to compel an individual to enter into such agreements, then the entering into such agreements cannot be insisted upon as a condition for agreeing to the principal contract or arrangement. German practice has been so notorious in this respect that special consideration should be given to abolishing immediately compulsory arbitration practices.

Allocations

Problem

The flow of materials through an economy has often been compared to the flow of blood through a living person. There is no doubt that the analogy is accurate in many respects. The ability to control the flow of materials in an economic system gives to the person or organization having such control the power of life or death over any concern dependent on the flow of such materials and also enormous control over the market place itself. The power of allocating scarce materials, if placed in the wrong hands, can create monopolies, put independent firms out of business, prevent the investment of new money, and crystalize the flow of materials into fixed and arbitrary channels. On the other hand the proper and intelligent operation of an allocation system could aid the German economy to convert to a healthy and balanced economy, could result in emphasis on the production of essential commodities rather than luxury goods, could insure distribution of available materials to a greater number of people and with greater equity, and so on.

Recommendation

That allocation standards be prescribed which would (a) prevent the delegation of allocation functions (i.e. government functions) to private groups, (b) guarantee adequate appeal procedures to persons discriminated against by such allocation procedure, (c) insure that complete records are made available both for purpose of government supervision and for the use of an individual who desires to use such records for his own protection, and (d) contain an early termination date, i.e. as soon as the item in question is reasonably available.

Discussion

Allocation measures should be used so far as possible only in a positive sense to achieve certain objectives, such as broad distribution of production equitable division of scarce items, encouragement of independence of action on the part of small and medium-sized enterprises, and prevention of monopolies and restrictive practices which might otherwise grow out of the condition of scarcity. Allocation measures and procedures should not be used to guide in a detailed fashion the method of production or exact other conditions not pertinent to an allocation program and should not permit

the tying up of raw materials. It should be clearly recognized that combines and cartels usually have special controls of raw materials. An allocation program can also be used to guide the allocation of labor, though such a purpose should never be the fundamental purpose for an allocation program. Allocation quotas should not be available for sale between businessmen such as, for instance often is the case of a franchise or a patent or some other privilege granted by a government.

F.O.B. - Price System

Problem

German industrialists and businessmen have developed in a major way the practice of using uniform-delivered and basing-point pricing systems. A uniform-delivered pricing system is one in which all consumers buy the product at the same price no matter where they are located in relation to the source of production. A basing point pricing system is one in which the producers agree to and do select a limited number of points, usually cities, from which transportation costs are added to determine the consumer price. That is, the consumer will be charged only the transportation cost from the nearest basing-point. Basing-point and uniform-delivered pricing systems are generally used for basic commodities. This conception of basing point and uniform-delivered pricing systems does not apply to an individual producer independently distributing his own products but is usually applied to concerted action by two or more producers. An individual producer can use any system he desires and it simply becomes his own system. Where such a system is imposed by a government for purportedly beneficial reasons, it represents at best a subsidy to a particular group of consumers and is always subject to the abuses stated below. If such subsidies are deemed essential they should be made effective by direct grants or other benefits to the favored group in question.

Recommendation

To prohibit and make illegal the using of uniform-delivered and basing-point pricing systems in Germany by requiring a system to be adopted in which prices are quoted f.o.b. factory or actual point of shipment by the seller.

Discussion

Uniform-delivered and basing-point pricing systems among other things foster monopoly, restrain trade, eliminate competition, conceal transportation costs, place price control into the hands of private groups and prevent purchasers from making price comparisons. They are in themselves monopolistic arrangements and are used by cartels, trusts and syndicates as aids in the furtherance of the domination and control of markets.

The quoting of a uniform-delivered or basing point price for a product discriminates against purchasers who are located near the center of production. Although differences in costs of transportation and handling exist, a purchaser 1,000 miles away from the factory may pay no more than a purchaser living

one mile away from the factory... Thus, in fertilizer and in steel, certain basing-points have been selected by producers as a convenient means of stating prices. Prices are quoted per ton at one or more points plus freight charges from these designated centers to destination. In practice, shipments of these commodities may be made from any geographical point of production, but prices are quoted in terms of location in one of the cities selected as a price basing-point. Discrimination here is geographic. The greater the freight cost per unit the more the discrimination against the consumer located near the actual point of production. Since it cannot be assumed that the producer will absorb the freight costs himself it must be assumed that he will average the total freight and charge it to his consumers regardless of their location. Consequently purchasers located near the center of production are penalized in the price they pay to the extent of the freight costs in shipping the goods at the same standard selling price to markets more distant from the actual point of production but the same distance from the arbitrarily selected "basing-point".

Under the uniform-delivered and basing-point pricing schedules the basic schedule price, less freight, is also usually set high enough to cover the cost of the least or the less effecient producer. Where suffucient cooperation exists in an industry to establish a basing-point system or the pooling and equalization of freight costs, such cooperation is usually also sufficient to establish price uniformity and price fixing. These methods allow unreasonably high and monopoly profits to the more efficient. Price competition is eliminated and quality and choice of products reduced. Suppliers are enabled to retain completely for themselves all benefits resulting from a reduction in the cost of production or distribution or from a reduction in quality, rather than being obliged to pass along to the consumer at least a part of any such reduction in cost.

From the point of view of the consumer, uniform-delivered or basing-point prices are subject to additional objections. The consumer is unable to benefit from any available alternative means of transportation even if he lives near the factory, or actual point at which the material is available, and has his own means of transportation; he does not know and cannot obtain knowledge of the actual cost of production or transportation of the product; he is prevented from selecting suppliers on the basis of price; and usually alternative products have been priced by agreement so that they are unavailable to him.

Foreign Trade

Problem

While the resumption of German foreign trade is an essential step in the reconstruction of a peaceful German economy, it will be necessary for the occupation authorities to supervise and control such trade for a long time to come and to reorient every phase of it to serve peaceful rather than aggressive purposes. For decades German foreign trade policy has been marked by private and governmental restrictions and restraints, all of which have helped to further German

aggression in the economic field, in times of peace as well as war. Tariffs were designed to strengthen agricultural and industrial self-sufficiency, bilateral trade agreements provided levers for the economic penetration of other countries, cartel agreements with foreign firms restricted the volume of foreign trade and the production potential of Germany's future enemies. Such practices reached their culmination under the Nazi regime when foreign trade operations and controls became an integral part of Germany's war effort.

Recommendation

That resumption of German foreign trade operations be allowed only with due regard to security considerations, and on a free and non-discriminatory basis in accordance with the principles laid down in the proposed charter for an International Trade Organization; that existing trade agreements, treaties and tariff schedules be revised to delete all exploitative features and to give maximum encouragement to the development of free and non-discriminatory trade; and that participation in international cartels by any person or enterprise in Germany be prohibited.

Discussion

The conduct of German foreign trade must for a long period be subject to control by the occupying forces to insure complete German disarmament and a basic reorientation of German foreign trade practices. It will be particularly important to prevent a resumption of restrictive practices between German and foreign cartels, nor must Germany be allowed to play off one of the Allies against another by means of discriminatory trade agreements or tariff rates. When Germany does return to normal commercial relations with the rest of the world, the standards prescribed for international commercial relations contained in the charter of the International Trade Organization of the United Nations should be adopted to guide future German conduct in international trade. These standards have already been agreed upon by a large number of nations and have been formulated to maximize the volume of international trade and the benefits to be derived therefrom for the economic well-being and political stability of all participating countries.

Emergency Import-Export Program

Problem

The large import balance so far financed by the United States and the British has led OMGUS to formulate a plan for, and to establish an import-export program. This program will, if successful, bring raw materials into Germany which will be combined with certain indigenous products for fabrication by German labor and capital equipment into finished products which will be exported and sold at high enough prices to cover at least the cost of the imported raw materials plus a dollar profit which will be made available to pay for occupation costs and necessary food imports (i.e. current trade deficits).

Germany's export program between the two wars was dedicated, in substantial part, to economic warfare and economic penetration of foreign countries. Hundreds of firms participated in this German effort, hundreds of trade-marks, trade names and patents were used in the implementation of such program. In view of the undesirability of continuing the trade practices pursued by German firms and some of their trade partners abroad before World War II, and the necessity of maintaining close supervision over German foreign trade during the emergency period, the Government agencies at Washington have made certain recommendations.

During the month of November 1946, for example, a policy was set forth directing that cartel-connected firms in Germany should be excluded from this import-export program until such firms were sufficiently reorganized to eliminate their cartel connections; lists of trade-marks and trade names which were to be excluded from such program were established; and specific policy directives were given as to tests to be used certain consignee firms outside of Germany from participation in the program. Firms known to be German-owned or controlled or subject to regulation under security programs and firms known to have persistently and wilfully aided the enemy during the war are to be excluded. Furthermore, exclusive contracts are to be discouraged, price fixing, allocation and other restrictive arrangements are to be avoided and prevented. Screening of potential consignees outside of Germany is to be accomplished.

Recommendation

That participation of all firms in the import-export program in or outside of Germany be subject to approval by the Decartelization Branch prior to or at any early stage in their participation in such program, and that no restrictive contracts be approved by Military Government.

Discussion

While the number of firms in Germany which might desire to participate in the import-export program may be fairly numerous, the number of ultimate actual participants in the program is not expected to be too numerous for effective screening. The use of a short form questionnaire to determine certain essential facts prior to participation by any firm is a standard operating procedure (used during the war) and has been used in many other programs. Military Government has in its files already a large amount of evidence concerning undesirable firms in Germany which might desire to participate in the subject program. Conditional permission could be given firms until they had modified their practices and structure sufficiently to gain complete acceptance by Military Government.

Firms outside of Germany which may wish to participate in this program should also be subject to immediate elimination from the program upon a finding that their inclusion would contravene the policies set out above.

Reparations

Problem

In order that Germany compensate some of the countries which were devastated by German armed forces during the war, it has been decided that certain reparations in the form of plants and machinery be made to such countries. The plants designated for reparations have been selected as those not necessary to the "level of industry" plan, i.e. particularly plants in those industries where Germany had excess production capacity, plant and equipment.

Reparations policy could very easily be used as a means of deconcentrating certain segments of the German economy. The plants of the large combines could be taken first. There are several reasons why plants of the large combines should, wherever possible, be among the first selected for reparations purposes. In the first place, they profited more than any other group in the German economy by the expansion for wartime production. Secondly, they may still be able to regroup the plants that remain to them into large combines and continue the same old practices. A small company, if its plant is dismantled, immediately goes out of business. Thirdly, if the German economy is to be decentralized, it is desirable that as many medium-sized enterprises as possible remain to permit the decentralization to be carried out without an unnecessarily large number of reorganizations.

In some parts of Germany, pressures are being applied already, which favor the large combines at the expense of smaller competitors. Newcomers to a field are discouraged from operating and production is limited to certain specified and standardized types, models, etc. based upon the production facilities of the large combines. Since the large combines, in some cases, had almost completely driven competition from the field, this means that the influx of new and competing enterprises becomes difficult, if not impossible.

Recommendation

Beneficial preference should be given to independent, medium-sized and smaller companies in designating plants for reparations purposes.

Discussion

The carrying out of this recommendation would serve to cut off from many of the largest combines many of their larger plants and properties. In doing so many cartel arrangements would have to be re-negotiated because certain parties to them would be eliminated, new producers would appear, and a general readjustment be necessitated. This overall reorganization, if decartelization principles are in force during such period, should bring into industry new capital, new management, new methods and new concepts of doing business. The ownership and control of the German economy would be spread into many more hands. The economy would gain flexibility and be more capable of absorbing new ideas, new inventions, of discarding obsolete equipment, and of responding to new market forces.

Taxation

Problem

The German corporate income, turnover and property taxes are of particular importance to the implementation of the decartelization program. Taxes may encourage or discourage the formation of large combines. They may encourage the use of the holding company device. They may force corporate relations into patterns which can be easily supervised, or at least make it difficult to maintain sub rosa relations.

German corporation taxes are several in number as are exemptions thereto. There is a tax on net corporate income, and a withholding tax on dividends actually paid out. Under the latter, called the Capital Yields Tax (Kapitalertragssteuer), the recipient of the dividend is required to report the amount so received as part of his taxable income. The recipient is permitted to deduct from his personal income tax (for corporation tax, in the case of corporations), those amounts which have been deducted by the company paying the dividend.

The "Schachtelprivileg" constitutes a tax exemption where one corporation (the parent) has an interest in another (subsidiary) corporation which exceeds 25 per cent of the capital stock of the subsidiary. This privilege is granted only to domestic corporations which have owned the interest in the subsidiary since the beginning of the fiscal year. The privilege affects the income tax payable by the parent corporation as well as the duty of the affiliate to withhold such tax at the source. Under the former German tax law, parent corporations claiming the Schachtelprivileg did not have to pay taxes on that part of their income which represented dividends received from subsidiaries. Moreover, the subsidiaries were not required to withhold the Capital Yields Tax on dividends paid to parents.

The Schachtelprivileg led to numerous abuses and encouraged the use of the subsidiary company device, leading to large holding company structures. Corporation taxes were lower when paid on the smaller profits represented by subsidiaries than on the larger profits of a unified, integrated, single corporation. Further, it was an incentive to corporations to exchange stock, in amounts of 25 per cent, in order to profit by lower taxes.

It was clearly the intention of the framers of Control Council Law No.12 (Article XV, Par.3) to abolish completely the Schachtelprivileg. However, apparently, because of an incomplete awareness of the extent of the tax privilege, only the exemption from withholding the tax on dividends was eliminated. The exemption granted to the parent from paying tax on its dividend receipts still remains. The fact that corporation tax rates have been increased to a maximum of 65 per cent only intensifies the advantage to combines.

Another abuse fostered by the former German tax law was the Organgesellschaft principle. By this arrangement, an Organgesellschaft relationship was deemed to exist when one company was financially economically and organizationally a part or "Organ" of another company and could no longer be con-

sidered independent. In addition, to qualify for such status an agreement was required providing for transfer of profits from the subsidiary to the parent company.

Organgesellschaften were privileged with regard to turnover taxes. In order to avoid pyramiding of turnover taxes, the latter were remitted on transactions between Organgesellschaften and their parents. Since these taxes ranged as high as 2½ per cent, and since independent firms not vertically integrated were required to pay a turnover tax at each stage of production, small, independent firms found themselves unable to compete against the combines. Turnover tax exemptions have now been abolished and turnover taxes raised.

However, the provision allowing the writing off of the losses of Organgesellschaften against the profits of the parent organization has not been abolished. Although the law provides that an Organgesellschaft relationship is to be recognized only where the parent organization is active in the same field as the controlled company, in practice, a firm like I.G. Farben was able to claim as Organgesellschaft almost any of its firms in the chemicals field and Siemens almost any of its firms in the electro-engineering field. An Organgesellschaft could drive smaller independent competitors to the wall by a policy of ruinous price-cutting, since any losses incurred thereby could be deducted, for tax purposes, from the profits of the controlling company. With the present sharply graduated tax scale, such a practice would be economically feasible and desirable to a corporation. It should be remembered that this privilege has no basis in any German legal enactment but was developed by decisions of the highest tax authorities, particularly by the so-called Reichsfinanzhof, the Supreme Finance Court of Germany. Consequently, a positive provision would be needed to abolish the privilege.

The German property tax (Vermoegensteuergesetz) was paid on net assets at a maximum rate of 5 per cent. This maximum rate, on net assets over RM 500,000, has been lowered by Control Council Law No.15 to 2½ per cent. No undistributed profits tax existed in Germany, nor does one exist at present. The property tax served, to some extent, the encouragement of a declaration of dividends. To allow a corporation to plow back into the corporation a large part of its earnings where a smaller or less diversified competitor must pay market prices for money places the smaller or less diversified corporation at a distinct disadvantage.

Recommendations

In order to aid in the effectuation of decartelization objectives, the following steps should be considered:

1. The raising of the property tax, at least as to large enterprises.

2. The establishment, at a proper time, of an undistributed profits tax to the extent necessary to prevent unreasonable ploughing back of earnings.

3. The prohibition of consolidated tax returns for any group of corporations, and the taxation of each cor-

poration as a separate unit.

4. The prohibition of carry-over tax provisions and a general simplification of tax measures and procedures.

Discussion

It is believed that the implementation, in Germany, of the suggested tax program would aid in the elimination of holding companies except where they are economically justifiable. Simple corporate relation patterns would be fostered which can be readily supervised, and tax privileges favoring holding companies and large, complex corporate relations would be eliminated.